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**82 -704**

Case No. .....

# In the Supreme Court of the United States

**October Term, 1982**

THE CLEVELAND ELECTRIC ILLUMINATING COMPANY,

*Appellant,*

vs.

THE PUBLIC UTILITIES COMMISSION OF OHIO,

and

OFFICE OF CONSUMERS' COUNSEL,

*Appellees.*

ON APPEAL FROM THE SUPREME COURT OF OHIO

## JURISDICTIONAL STATEMENT

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## QUESTIONS PRESENTED

1. May the State of Ohio, by statute, constitutionally require a public utility to invest its capital for the convenience of the public to provide adequate service in the future and simultaneously prohibit, by statute, that utility from recovering through rates such capital when prudently invested?

2. May the State of Ohio, by statute, constitutionally prohibit a public utility from recovering through rates its capital, prudently invested for the convenience of the public, where the undisputed facts show that the utility, and its investors, have never been compensated through the authorized rate of return for the risk of exclusion of such costs from rates?

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## ADDITIONAL AUTHORITIES CITED TO THE OHIO SUPREME COURT

The following authorities were provided to the Ohio Court to show that the overwhelming weight of modern authority supports amortization, as noted in footnote 19 at page 27, *infra:*

FEDERAL ENERGY REGULATORY COMMISSION: *Southern Ca. Ed. Co.*, Opn. No. 821, Dkt. No. E-8176, 23 P.U.R. 4th 44 (Fed. Pwr. Comm., 9/22/77); *Jersey Cen. Pwr. & Lght. Co.*, Dkt. No. ER76-813 (FERC, 3/27/78); *Louisiana Pwr. & Lgt. Co.*, Dkt. No. ER77-533 Phase I (FERC, 2/12/79); *New Eng. Pwr. Co.*, Opn. No. 49, Dkt. Nos. ER76-304, ER76-317, ER76-498, 18 FPS 5-484 (FERC, 7/19/79), affirmed in part and remanded on other grounds, *NEPCO Municipal Rate Committee et al. v. FERC et al.*, 668 F.2d 1327 (D.C. Cir., Oct. 15, 1981), *cert. den.* 50 U.S. Law Week 3978 (6/15/82); *Northern States Pwr. Co. (Minn.) – Northern States Pwr. Co. (Wis.)*, Dkt. No. ER79-616, 17 FERC, ¶ 61,196 (FERC, 12/4/80 and 12/3/81); *Union Electric Co.*, Opn. No. 94, 12 FERC (CCH) ¶ 61,239, *aff'd*, 668 F.2d 389 (8th Cir., 1981);

ALABAMA: *Alabama Pwr. Co.*, Dkt. No. 17667 (Ala. Pub. Serv. Comm.);

CALIFORNIA: *San Diego G. & Elec. Co.*, Case No. 90405, 31 P.U.R. 4th 435 (Ca. Pub. Util. Comm., 6/5/79); *Southern Ca. Ed. Co.*, Case No. 81919 (Ca. Pub. Util. Comm., 8/1/72); *Southern Ca. Ed. Co.* Case No. 86794 (Ca. Pub. Util. Comm., 6/7/74); *Southern Ca. Ed. Co.*, Decision No. 89711 (Ca. Pub. Util. Comm., 12/ /78);

DISTRICT OF COLUMBIA: *Potomac Elec. Co.*, Case No. 685, Order No. 6096, 29 P.U.R. 4th 517 (D.C. Pub. Serv. Comm., 6/14/79);

FLORIDA: *Gulf Power Co. v. Cresse*, 410 So.2d 492 (Florida S.Ct, 1/28/82), affirming *Gulf Power Co.*, Docket No. 800001-EU(CR) (Fla. Pub. Serv. Comm., 11/10/80);

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MICHIGAN: *Consumer Pwr. Co.*, Case No. F-700 (Mich. Pub. Serv. Comm., 2/10/75); *Detroit Ed. Co.*, Case No. F-762 (Mich. Pub. Serv. Comm., 7/26/76); *Detroit Ed. Co.*, Case No. U-5108 (Mich. Pub. Serv. Comm., 5/27/77);

MISSOURI: *Union Elec. Co.*, Case No. ER77-154 (Mo. Pub. Ser. Comm., 1/19/78);

NEW JERSEY: *Pub. Serv. Elec. and Gas Co.*, Dkt. No. 794-310 OAL Dkt. No. PUC 877-79, 37 P.U.R. 4th 631 (N.J. Dept. of Egy., Bd. of Pub. Util., 4/11/80); *Hope Creek Investigation*, Docket No. 8012-914 (N.J. Dept. of Egy., Bd. of Pub. Util., 4/1/82), CCH Utilities Law Reports-State, ¶ 23,634;

NEW YORK: *New York State Elec. & Gas Corp.*, Case Nos. 26432 and 26433, Opinion No. 74-12, 14 NY PSC 564, and Case Nos. 26763 and 26764, Opinion No. 75-24, 15 NY PSC 1564 (N.Y. Pub. Serv. Comm., 4/10/74); *Consolidated Edison Co.*, Case 27744, Opinion 81-4 (N.Y. Pub. Serv. Comm., 3/12/81); *Rochester Gas and Elec. Corp., et al.*, Opn. No. 82-1, Case No. 27794 (N.Y. Pub. Ser. Comm., 1/12/82);

NORTH CAROLINA: *Carolina Pwr. & Lgt. Co.*, Dkt. No. E-2, Sub. 366 (N.C. Util. Comm., 4/22/80);

NORTH DAKOTA: *Northern States Power Co. v. North Dakota Pub. Serv. Comm.*, 314 N.W.2d 32 (North Dakota S.Ct., 12/22/81);

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SOUTH DAKOTA: *Northern States Pwr. Co.*, Decision and Order No. F-3062 (S.D. Pub. Util. Comm., 10/6/76);

TEXAS: *Gulf States Util. Co.*, Dkt. No. 2677 (Tex. Pub. Util. Comm., 10/29/79; *Houston Lgt. & Pwr. Co.*, Dkt. No. 2001 (Tex. Pub. Util. Comm., 12/5/78); *Houston Lgt. & Pwr. Co.*, Dkt. No. 2676 (Tex. Pub. Util. Comm., 1/9/80);

VIRGINIA: *Virginia Elec. & Pwr. Co.*, Case No. 19960, 29 P.U.R. 4th 65 (Va. Corp. Comm., 3/19/79);

WEST VIRGINIA: *Appalachian Power Co.*, Case No. 9091 (W. Va. Pub. Serv. Comm., 5/3/78); *Virginia Elec. and Power Co.*, Case No. 9322 (W. Va. Pub. Serv. Comm., 2/1/80); *Virginia Elec. and Power Co.*, Case No. 81-413-E-42T (W. Va. Pub. Serv. Comm., 5/21/82);

WISCONSIN: *Wisconsin Pub. Serv. Corp. v. Pub. Serv. Comm.*, Case No. 79CV809 (Wisc. Cir. Ct. II, 10/15/79), *rev'd*, Ct. of App. Dist. III, Case No. 79-1929, 10/7/80); *Wisconsin Electric Power Co.*, Case No. 05-CE-3, 40 P.U.R. 4th 630, 688 (Wisc. Pub. Serv. Comm., 2/14/80)

The following authorities were cited to the Ohio Court to show that the overwhelming weight of prior authority supports amortization:

CALIFORNIA: *Calif. Farm Bureau Fed. v. San Joaquin Lt. & Pwr. Corp.*, P.U.R. 1932D, 310, 326 (Calif. R.R. Comm., 1932); *San Diego Transit Sys.*, 88 P.U.R. (n.s.) 459, 468 (Cal. Pub. Util. Comm., 1951);

DISTRICT OF COLUMBIA: *Washington Gas Light Co.*, 83 P.U.R. (n.s.) 4, at 19 (D.C. Pub. Util. Comm., 1949, referring explicitly to Account 506, Property Losses Chargeable to Operations), *aff'd in part and rev'd and remanded in part*, 188 F.2d 11 (D.C. Cir., 1950), *cert. den.* 340 U.S. 952 (1951);

FLORIDA: *Jacksonville Gas Corp.*, 40 P.U.R. 3d 372, 374-75 (Fla. R.R. and Pub. Util. Comm., 1961);

GEORGIA: *Walker County Tel. Co.*, 86 P.U.R. (n.s.) 61, 62-63 (Ga. Pub. Serv. Comm'n., 1950);

MARYLAND: *Eastern Shore Pub. Serv. Co.*, P.U.R. 1931E, 363 (Maryland Pub. Serv. Comm., 1931);

MICHIGAN: *Michigan Consol. Gas Co.*, 22 P.U.R. 3d 369, 375-77 (Mich. Pub. Serv. Comm., 1958);

MINNESOTA: *Minneapolis Street Rwy. Co. v. City of Minneapolis*, 251 Minn. 43, 86 N.W.2d 657, 668 (1957);

MISSOURI: *Bolivar Tel. Co.*, 43 P.U.R. 3d 417, 419-20 (Mo. Pub. Serv. Comm'n., relying explicitly on the applicable Uniform System of Accounts, 1962); *St. Joseph Ry. Lt. Ht. & Pwr. Co.*, 5 P.U.R. (n.s.) 253 (Mo. Pub. Serv. Comm., 1934);

MONTANA: *Pub. Serv. Comm. v. Great Northern Util. Co.*, P.U.R. 1929B, 176 (Mont. Pub. Serv. Comm., 1929);

NEBRASKA: *Lincoln Traction Co.*, 43 P.U.R. (n.s.) 535 (Neb. Pub. Serv. Comm., 1940);

NEVADA: *Henderson Tel. Co.*, 41 P.U.R. 3d 248, 253 (Nev. Pub. Serv. Comm'n., 1961);

NEW YORK: *Consolidated Edison Co.*, 56 P.U.R. 3d 377, 3-71-75 (N.Y. Pub. Serv. Comm., 1964);

NORTH CAROLINA: *Mebane Home Tel. Co.*, 29 P.U.R. 3d 222, 224 (N.C. Util. Comm'n., 1959);

PENNSYLVANIA: *Franke v. Johnstown Tel. Co.*, P.U.R. 1929D, 161, 164-165 (Penn. Pub. Serv. Comm., 1929); *Penn. Pub. Util. Comm. v. North Penn Gas Co.*, 60 P.U.R. (n.s.) 331 (Penn. Pub. Util. Comm., 1945);

WASHINGTON: *Washington Pub. Serv. Comm. v.* Northwest Nat. Gas Co., 32 P.U.R. 3d 355, 360-61 (Wash. Pub. Serv. Comm., 1960);

WISCONSIN: *City of Racine v. Wisconsin Nat. Gas Co.*, 100 P.U.R. (n.s.) 467, 473-75 (Wisc. Pub. Serv. Comm., 1953); *Re Shell Lake Tel. Co.*, 36 P.U.R. 3d 413, 416 (1960); and *Re Rock River Tel. Co.*, 37 P.U.R. 3d 49, 52 (1960), both Wis. Pub. Serv. Comm'n.

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## REPORTS OF OPINIONS BELOW

The decision of the Ohio Supreme Court dated July 7, 1982 dismissing this case without explanation is not officially reported. The Court's denial, again without explanation, of Appellant's Motion For Rehearing, dated July 29, 1982, is also not officially reported. The *Opinion and Order* of the Public Utilities Commission of Ohio in Case No. 81-1096-EL-COI dated October 21, 1981 is not officially reported. The Commission's Entry on Rehearing from that decision dated December 9, 1981 is not officially reported.

The related decision of the Ohio Supreme Court dated July 15, 1981 in *Consumers' Counsel v. Pub. Util. Comm.* (*CEI*), is reported at 67 Ohio St. 2d 153, 423 NE. 2d 820 (1981).[1] The Court's denial of Appellant's Motion For Rehearing from that decision is not officially reported. The Court's denial of Appellant's Motion For Stay is not officially reported. The related *Opinion and Order* of the Public Utilities Commission of Ohio in Case No. 79-537-EL-AIR dated July 10, 1980 is reported at 38 PUR 4th 494 (1980). The Commission's Rehearing Entry dated September 3, 1980 in that case is not officially reported. A copy of each of these decisions is included in the separate Appendix.

## GROUNDS FOR JURISDICTION

This appeal is brought to review a decision of the Ohio Supreme Court dismissing Appellant's appeal from an *Opinion and Order* of the Public Utilities Commission of Ohio reducing Appellant's rates for electric utility service to retail customers in Ohio.

Jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1257(2) to review the final judgment rendered on July 7, 1982 by the Ohio Supreme Court, the highest court of the State of Ohio. Appellant's Motion for Rehearing was denied by the Ohio Supreme Court on July 29,

[1]Hereinafter cited as *Consumers' Counsel.*

1982. Appellant filed its Notice of Appeal with the Ohio Supreme Court on October 15, 1982.

The validity of Ohio Revised Code Sections 4905.22 and 4909.15(A)(4) was drawn into question before the Ohio Supreme Court on the grounds that, as construed and applied, they are repugnant to the Fifth and Fourteenth Amendments to the Constitution of the United States, and the decision of the Ohio Supreme Court was in favor of the validity of those statutes.

In the event that an appeal is not considered the proper mode of review, Appellant requests that the papers upon which this appeal is taken be regarded and acted upon as a petition for writ of certiorari pursuant to 28 U.S.C. § 2103.

## CONSTITUTIONAL PROVISIONS, STATUTES, AND REGULATIONS INVOLVED

1. The Fifth Amendment to the Constitution states, in pertinent part, as follows:

> "No person shall be . . . deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation."

2. The Fourteenth Amendment to the Constitution states, in pertinent part, as follows:

> "No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law. . . ."

3. Ohio Revised Code § 4905.22, states, in pertinent part, as follows:

> "Every public utility shall furnish necessary and adequate service and facilities, and every public utility shall furnish and provide with respect to its business such instrumentalities and facilities as are adequate and in all respects just and reasonable."

4. Ohio Revised Code § 4909.15, states, in pertinent part, as follows:

> "(A) The public utilities commission, when fixing and determining just and reasonable rates, fares, tolls, and charges shall determine:
>
> • • •
>
> (4) The cost to the utility of rendering the public utility service for the test period. . . ."

5. Ohio Administrative Code § 4901:1-9-05, Uniform Classification of Accounts for Electric Utilities – FPC, 1961 states, in pertinent part:

> "The system of accounts and records, identified and designated as "Uniform System of Accounts Prescribed for Public Utilities and Licenses, effective January 1, 1961," as adopted by the Federal Power Commission, is adopted by this Commission effective as of January 1, 1961, for electric light companies operating within the state of Ohio which are subject to the jurisdiction of the Federal Power Commission. . . . Each such public utility shall carry on its books, in addition to such additional accounts as may hereafter be prescribed by this Commission, the accounts and records prescribed in said Uniform System of Accounts effective January 1, 1961, for a public utility of its class, and shall accordingly keep such accounts in accordance with the requirements, definitions and instructions contained and set forth in said uniform system of accounts. . . ."

6. FERC Uniform System of Accounts, 18 C.F.R. 101, Definitions, p. 288 states, in pertinent part:

> "8. "Cost" means the amount of money actually paid for property or services. . . ."

7. FERC Uniform System of Accounts, 18 C.F.R. 101, Electric Plant Instructions, ¶ 4, Overhead Construction Costs, p. 300 states, in pertinent part:

"A. All overhead construction costs, such as engineering, . . . construction engineering and supervision by others than the accounting utility, law expenses, insurance, injuries and damages, relief and pensions, taxes and interest, shall be charged to particular jobs or units. . . ."

8. FERC Uniform System of Accounts, 18 C.F.R. 101, Balance Sheet Chart of Accounts, Assets and Other Debits, Account 107, Construction Work In Progress — Electric, p. 313 states, in pertinent part:

"A. This account shall include the total of the balances of work orders for electric plant in process of construction.

B. . . . Any expenditures which are identified exclusively with units of property not yet in service shall be included in this account."

9. FERC Uniform System of Accounts, 18 C.F.R. 101, Balance Sheet Chart of Accounts, Assets and Other Debits, Account 182, Extraordinary Property Losses, p. 324 states:

"A. When authorized or directed by the Commission, this account shall include extraordinary losses on property abandoned or otherwise retired from service which are not provided for by the accumulated provisions for depreciation or amortization and which could not reasonably have been foreseen and provided for, and extraordinary losses, such as unforeseen damages to property, which could not reasonably have been anticipated and which are not covered by insurance or other provisions."

## STATEMENT OF THE CASE

### A. The facts material to the questions presented.

The underlying facts are known to the Court and are set out in detail in the Ohio Supreme Court's Opinion in *Consumers' Counsel* as well as in the decisions of the

Public Utilities Commission of Ohio ("Commission") in PUCO Case Nos. 79-537-EL-AIR and 81-1096-EL-COI and the briefs of the parties in the prior appeal to this Court (Case No. 81-1002). They need, therefore, be only briefly reviewed here in order to put the legal issues in context.

Appellant, The Cleveland Electric Illuminating Company ("CEI") is an electric utility rendering service in northeastern Ohio. It is regulated in various respects by the Public Utilities Commission of Ohio and is obligated, by Ohio Revised Code Section 4905.22 to furnish necessary and adequate facilities for the reliable rendition of service in its territory to all who seek it, both now and in the future.

In 1967, The Cleveland Electric Illuminating Company joined with four other electric utilities (Ohio Edison, Toledo Edison, Duquesne Light and Pennsylvania Power) in an organization, the Central Area Power Coordination Group ("CAPCO"), for the joint planning, construction and operation of "base load" generation capacity; i.e., very large generating units intended to be less expensive to operate at a relatively constant level of production. Such units require extremely long construction lead times and, therefore, must be planned and committed many years in advance.

In early 1973, the CAPCO companies, acting on the best forecasts and information available, entered into commitments to construct four nuclear units — Davis-Besse Units №2 and №3 and Erie Units №1 and №2 — in order to supply the required adequate amount of electric power to the public in 1983 and thereafter. The Commission found that this decision was prudent.

Pursuant to that decision, CEI (with its CAPCO partners) began expending its capital to plan, engineer and begin initial construction of the four units. Subsequent

developments, not the least of which was the Arab Oil Embargo (which no one could have predicted) resulted in a reduction of the forecasted rate of growth in the demand for power in the CAPCO area. The Commission found that CEI's decisions to continue planning and engineering expenditures were prudent.

Yet another unanticipated factor was added in early 1979, when the Three-Mile Island ("TMI") incident resulted in sharply increased political and regulatory uncertainty regarding the construction and operation of nuclear generating plants. The TMI unit was constructed by Babcock and Wilcox, the same company which had already constructed a licensed and operating nuclear generation unit known as Davis-Besse Unit #1 for some of the CAPCO companies, including CEI. Before TMI, it had been anticipated that Davis-Besse Unit #1 would be duplicated in constructing the other four planned units, with attendant savings.

However, after TMI, it became apparent that the substantial savings of time and money anticipated by CAPCO from duplicating the existing Davis-Besse Unit #1 when Davis-Besse #2 and #3 and Erie #1 and #2 were constructed would not occur. Davis-Besse #2 and #3 and Erie #1 and #2 were exposed to drastic design change requirements and to unpredictable future licensing, design, construction, and operation requirements by the Nuclear Regulatory Commission.

These considerations caused CEI and its CAPCO partners to terminate planning for the four units on January 23, 1980[3]. At that time, CEI had dedicated $56,437,000.00

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[3]The cancellation of these units did not result in a complete cessation of the CAPCO construction program. There are other base load generating units still under construction.

toward planning, engineering and initial construction costs on those units.[4] The Commission found that the decision to terminate was prudent.

On June 19, 1979, Appellant had served and filed a Notice of Intent to submit a rate increase application to the Commission, which had assigned to that Notice Case Number 79-537-EL-AIR (the "1979 Case").[5] After regular investigation by the Commission's Staff, hearings began on April 12, 1980 and lasted 32 trial days.

On July 10, 1980, the Commission issued its *Opinion and Order* in Case No. 79-537-EL-AIR granting CEI an increase in rates. The Commission accepted the recommendation of its Staff and authorized as a part of allowable costs for rate-making purposes the amortization[6] of the costs for planning, engineering, and initial construction associated with the four nuclear generating units which had been cancelled and abandoned on January 23, 1980.

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[4]The other utilities belonging to CAPCO had also dedicated substantial amounts to planning the four cancelled plants. Ohio Edison had dedicated approximately $85.5 million. Toledo Edison had dedicated approximately $24.5 million. Duquesne Light had dedicated approximately $35 million. Pennsylvania Power had dedicated approximately $16 million.

[5]A chart setting out the relevant dates of all Appellant's electric rate cases before the Ohio Commission and the Ohio Court, from Case No. 79-537-EL-AIR to the present, is attached hereto as Exhibit I for the Court's convenience.

[6]The Uniform System of Accounts, Definitions: "4. "Amortization" means the gradual extinguishment of an amount in an account by distributing such amount over a fixed period, over the life of the asset or liability to which it applies, or even the period during which it is anticipated the benefit will be realized." The Uniform System of Accounts is discussed *infra*.

The Commission allowed amortization of $56,437,000.00 in expenses over ten years.[7]

The Ohio Office of Consumers' Counsel ("OCC") and other intervenors in the Commission proceeding appealed the Commission's decision to the Ohio Supreme Court (Cases Nos. 80-1480, 80-1528, and 80-1547). CEI participated in that appeal as Intervening Appellee. On July 15, 1981, the Ohio Court, in a 5-2 decision, reversed and remanded the July 10, 1980 *Opinion and Order* of the Commission, holding that even where, as here, a capital expenditure for planning future utility service was required by Ohio Revised Code § 4905.22 for the convenience of the public and was prudent, the Commission nevertheless had no discretion to allow "the return *of* capital invested in failed projects" (67 Ohio St.2d at 167) as a "cost" under Ohio Revised Code § 4909.15(A)(4), as then construed for the first time by that Court. *Consumers' Counsel v. Pub. Util. Comm. (CEI)*, 67 Ohio St.2d 153, 423 N.E. 2d 820 (1981).

The Ohio Court has recently held that in *Consumers' Counsel* it announced "new law." *Consumers' Counsel v. Pub. Util. Comm. (Toledo Edison)*, 1 Ohio St.3d 22, at 24, 437 N.E.2d 586 (1982).

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[7]In effect, CEI was authorized to restore the investment to the investor over a ten year period, similar to the recovery of the investment which would have been achieved through depreciation over the life of the plants if they had gone into service. *See* Ohio Revised Code § 4905.18, which expressly provides for recovery of depreciation expense by the investor.

On July 24, 1981, CEI filed its Motion for Rehearing with the Ohio Court.[8] On September 1, 1981, that Court denied the Motion for Rehearing with a standard form Entry. On September 2, 1981, CEI filed with the Ohio Court its Notice of Appeal to this Court and a Motion for Stay. The Ohio Court denied the Motion for Stay with a standard form Entry on September 11, 1981.

By the time of the Ohio Court's decision in *Consumers' Counsel* reversing and remanding PUCO Case No. 79-537-EL-AIR to the Commission to eliminate the expenses involved, the Commission had already issued its *Opinion and Order* in CEI's subsequent rate case, PUCO Case No. 80-376-EL-AIR (the "1980 Case"), so the rates in effect at the time of the *Consumers' Counsel* decision had been established pursuant to the 1980 case. In establishing the 1980 Case, the Commission had again included as an allowable expense the amortization of the four cancelled units. Although OCC was a party to the 1980 case, and although the case was appealed to the Ohio Court on other issues, *see Senior Citizens Coalition v. Pub. Util. Comm.*, 69 Ohio St.2d 625, 433 N.E.2d 583 (1982), *no* party appealed the Commission's decision allowing the amortized amount of the cancelled units as an allowable expense.

Faced with the Ohio Court's remand in *Consumers' Counsel*, the Commission then instituted on September 16, 1981, on its own motion, PUCO Case No. 81-1096-EL-

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[8]Amortization of Ohio Edison's cancellation costs had been allowed in *Ohio Edison Co.*, PUCO Case No. 80-141-EL-AIR (*Opinion and Order*, April 9, 1981). Within days of the Ohio Court's July 15, 1981 decision in *Consumers' Counsel*, and as a direct result of its holding, the Commission granted to Ohio Edison, with the express consent of OCC, emergency rate relief in the annualized amount of $90,000,000, to offset the financial consequences resulting to that member of CAPCO. *Ohio Edison Co.*, PUCO Case No. 81-989-EL-AEM (*Opinion and Order*, July 31, 1981).

COI.[9] On September 22, 1981, CEI filed with this Court its Application For Stay of Execution And Enforcement of the Judgement of the Ohio Court. (Case No. A-250). This Court denied the requested Stay on October 12, 1981.

By its *Opinion and Order* dated October 21, 1981 ("the COI Order"), the Commission reduced CEI's rates for electric service by the amount which it had included in those rates in Case No. 80-376-EL-AIR with respect to the cancelled units, without any consideration of CEI's then-current revenues, expenses, or rate of return. Appellant CEI then appealed to the Ohio Court, arguing, among other things, that the Commission's COI Order reducing its rates was an unconstitutional confiscation of its property, while simultaneously briefing its appeal to this Court from *Consumers' Counsel*. Presented with the representation by OCC that the constitutional issue had *not* been decided by the Ohio Court, this Court dismissed Appellant's appeal "for want of a properly presented federal question" on January 25, 1982. *The Cleveland Electric Illuminating Company v. Office of Consumers' Counsel, et al.*, United States Supreme Court Case No. 81-1002, (February 25, 1982).

Only then did OCC move to intervene in CEI's appeal to the Ohio Court from the Commission's COI Order and move to dismiss, on the ground, *inter alia*, that the Ohio Court had *already* decided the constitutional issue.[10] The Ohio Supreme Court then dismissed with a standard form Entry on July 7, 1982. Appellant's Motion for Rehearing was similarly denied without opinion on July 29, 1982. Appellant CEI now appeals to this Court from the Ohio Court's July 7, 1982 dismissal.

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[9]"COI", in the Commission's case number abbreviations, stands for "Commission Ordered Investigation."

[10]OCC moved to intervene on April 28, 1982 and moved to dismiss on May 5, 1982.

Appellant has had yet another rate case, PUCO Case No. 81-146-EL-AIR (the "1981 Case"), which was decided by the Commission on March 17, 1982. In that case, the Commission refused to allow amortization of the cancelled units as an expense, *solely* because of the Ohio Court's decision in *Consumers' Counsel:*

> "Applicant has requested an allowance for ratemaking purposes for the amortization of the costs incurred with respect to four canceled nuclear units. This subject was fully discussed in *Cleveland Electric Illuminating Company,* Case No. 79-537-EL-AIR, Opinion and Order, July 10, 1980, in which the Commission approved such an amortization. The Commission approved the same amortization in applicant's subsequent rate case, *Cleveland Electric Illuminating Company,* Case No. 80-376-EL-AIR, *supra,* and approved a similar amortization in *Ohio Edison,* Case No. 80-141-EL-AIR, Opinion and Order, [February 11, 1981]. The Commission would approve the amortization again if it were not constrained by the decision of the Supreme Court of Ohio in *OCC v. Public Utilities Commission,* 67 Ohio St. 2d 153 (1981). This case clearly holds that this expense is, as a matter of law in Ohio, not includable as an operating expense for ratemaking purposes. The Commission must, therefore, deny applicant's request."

The 1981 Case is presently pending before the Ohio Court on CEI's appeal from the Commission's denial of the amortization as quoted above, and OCC has again intervened.

**B. The stage at which the question sought to be reviewed was raised below.**

CEI alerted the Ohio Court in its first brief (as an intervening appellee) in *Consumers' Counsel* of the then hypothetical constitutional problem which might arise if the Ohio ratemaking scheme were construed to prohibit recovery, as an expense, of required capital expenditures

found to be prudent. CEI cited and quoted the dissenting opinion of Commissioner Shannon in *Re: Virginia Electric & Power Company*, 29 PUR 4th 65(1979), where the Virginia Commission had allowed only amortization of the cancellation expenses:

> "Perhaps a more succinct way to state the proposition would be as follows: The investor is *constitutionally* entitled to *just compensation* for prudent expenditures. The ratemaking mechanism must provide for a return *on* the investment and the return *of* the investment. Because depreciation rates are not calculated to include the probabilities of extraordinary property losses, it is necessary to amortize the loss of Surry Units 3 and 4. Further, because rates of return have not compensated the investor for the risk of this extraordinary property loss, the unamortized balance should be included in the Company's rate base until the loss is completely amortized." (29 PUR 4th at 96, emphasis added).

CEI was, therefore, surprised by the Ohio Court's novel and unprecedented opinion – which the Ohio Court has itself described as announcing "new law"[11] – construing the word "cost" in Ohio Revised Code § 4909.15(A)(4) to prohibit the Commission from allowing even the recovery *of* (much less earnings *on*) necessary and prudent planning costs required by Ohio Revised Code § 4905.22. CEI explicity attached the validity under the Fifth and Fourteenth Amendments of those particular statutes, construed by the Ohio Court in *Consumers' Counsel*, at its earliest opportunity *after* this unconstitutional declaration of "new law" was rendered, in its Motion for Rehearing[12]

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[11] *See Consumers' Counsel v. Pub. Util. Comm. (Toledo Edison)*, 1 Ohio St.3d 22, at 24, 437 N.E.2d 586 (July 14, 1982).

[12] A copy of CEI's Motion for Rehearing has previously been supplied to this Court as Exhibit 3 to CEI's Application For Stay. (Case No. A-250).

to the Ohio Court filed on July 24, 1981. The Ohio Court appeared to decide in favor of the constitutionality of Ohio Revised Code § 4905.22 and § 4909.15(A)(4) when it decided against Appellant's Motion for Rehearing on September 1, 1981.

On CEI's appeal to this Court, this Court dismissed "for want of a properly presented federal question."

CEI clearly presented this federal question of the constitutionality of the Ohio statutes, as construed, in its appeal to the Ohio Court from the Commission's COI Order reducing CEI's rates. The Ohio Court dismissed that appeal without opinion. In CEI's Motion for Rehearing the Ohio Court was asked to clarify its decision, since it had 1) failed to address the constitutional issue in its initial decision in *Consumers' Counsel*, 2) failed to address the constitutional issue in denying CEI's Motion for Rehearing with a form Entry on September 1, 1981, 3) failed to address the constitutional issue in denying CEI's Motion to Stay, and 4) failed to address it a fourth time in dismissing CEI's present appeal from the COI order reducing its rates.

The Ohio Court rejected (for the fifth time) CEI's plea for some indication of its reasoning and denied CEI's Motion for Rehearing in this matter with a standard form Entry dated July 29, 1982.

CEI has raised the constitutional issue at least five times to the Ohio Court and has been unable to persuade that Court to address the issue at all.

## REASONS REQUIRING PLENARY CONSIDERATION

### I. OHIO REVISED CODE § 4905.22 AND § 4909.15(A)(4), AS CONSTRUED BY THE OHIO COURT, DIRECTLY CONFLICT WITH THE PROSCRIPTION OF THE FIFTH AND FOURTEENTH AMEND-

**MENTS TO THE CONSTITUTION OF THE UNITED STATES PROHIBITING CONFISCATION OF PRIVATE PROPERTY WITHOUT DUE PROCESS OF LAW.**

Ohio Revised Code § 4905.22 and § 4909.15(A)(4) may not constitutionally require a public utility to invest its capital in the present to provide adequate service to the public in the future and simultaneously deny recovery of that invested capital where it is found that the capital was prudently and reasonably invested for the convenience of the public for planning, engineering, and initial construction of electric generating units pursuant to the statutory requirement.

Ohio Revised Code § 4905.22, states, in pertinent part, as follows:

> "Every public utility *shall furnish* necessary and *adequate* service and *facilities*, and every public utility shall furnish and provide with respect to its business such instrumentalities and facilities as are adequate and in all respects just and reasonable." (emphasis added).

There is no question that this statute requires Appellant, as a public utility, to invest its capital in the present for planning and engineering for the convenience of the public to furnish adequate facilities in the future. The plain words of the statute say so, and the Ohio Court so held in *Consumers' Counsel*. The Ohio Court reiterated its stated view that "utilities *must anticipate* load growth years in advance to maintain adequate capacity to *ensure* reliable service . . ." (67 Ohio St.2d at 158, emphasis added).[13] An electric utility serving 700,000 customers obviously cannot operate without planning and engineering for the

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[13] *See also* Ohio Revised Code § 4905.20, which prohibits abandonment of utility facilities without Commission approval.

future. Large base load generating units, which have the advantage of being energy efficient, simply cannot be built without a lead-time exceeding ten (10) years.[14] The Commission found that the expenses at issue were proper business expenses which were prudently incurred.

Likewise, there is no question in this case that the capital invested by CEI for planning and engineering these generating units was dedicated to the convenience of the public as required by this Ohio statute. The Commission noted that "What the company seeks is the recovery of costs incurred on behalf of its rate payers to assure that adequate service could be maintained." (Quoted by the Ohio Court, 67 Ohio St. 2d at 161).

There is also no question as to the holding of the Ohio Court in *Consumers' Counsel*. It assumed that CEI's expenditures were required by Ohio Revised Code § 4905.22. It assumed they were prudently incurred. *Nonetheless*, the Ohio Court held that the Ohio ratemaking formula prohibits "the return *of* capital invested in failed projects. . . ." (67 Ohio St. 2d at 167).

Similarly, there is no question in this case regarding the accounting procedures imposed upon CEI by Ohio law and relied upon by CEI when it dedicated its capital to these projects. In 1937 the Federal Energy Regulatory Commission (then the Federal Power Commission)

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[14]The common law has for decades clearly required public utilities to anticipate future growth in demand and to take reasonable measures to meet that demand. *See Lukrawka v. Spring Valley Water Co.*, 169 Cal 318, 146 Pac. 640, PUR 1915 B 331 (1915) (a public utility must "anticipate the natural growth of the municipality . . . and take reasonable measures . . . to meet the reasonable demands . . . by the growing community." (146 Pac. at 643)); *People ex rel. Woodhaven Gas. Co. v. Deeham*, 153 N.Y. 528, 47 N.E. 787 (1897) ("It is well known that [utilities] are based upon calculations of future growth and expansion." (47 N.E. at page 788)); *Industrial Gas Co. v. Pub. Util. Comm.*, 135 Ohio St. 408, 21 N.E.2d 166 (1939).

adopted a Uniform System of Accounts, and required utilities subject to its jurisdiction, including CEI, to use it. *See* 18 C.F.R. 101 (1937). The Commission, pursuant to its authority under Ohio Revised Code § 4905.13, also adopted it, effective January 1, 1961, and required Ohio utilities, including CEI, to use it. *See* Ohio Administrative Code § 4901:1-9-05.

For the entire period from 1973 to 1979 during which CEI was spending this money, CEI was required by law to account for this money in certain ways, which it did. This Uniform System of Accounts defined "cost" to mean "the amount of money paid for property or services," (Definitions, ¶ 8), and described in detail the accounting procedures required for overhead construction costs like those involved here. (*See* Electric Plant Instructions, ¶ 4). Indeed, this Uniform System of Accounts sets out in great detail, under a separate heading, instructions to be used to account for "operating expenses" (*See* Operating Expense Instructions, at 18 CFR 101, pp. 309-310), prescribing some 400 separate Operation and Maintenance Expense Accounts (*See* 18 CFR 101, at pp. 366-392, Account Nos. 500-932).

The Uniform System of Accounts was and is the law in Ohio regarding utility accounting procedures. Under it, Overhead Construction Costs such as those involved here could *not* be shown on CEI's books as current operating expenses when made, although they were obviously necessary for the future operation of CEI. Instead, CEI had no choice but to capitalize the investment to Account 107, Construction Work In Progress, for the particular unit under construction, *See* 18 CFR Electric Plant Instructions, ¶ 4, Overhead Construction Costs, p. 300, and to defer any recovery *of* or *on* these expenditures until the units were recognized in rate base as part of Account 101, Plant in Service. From 1973 until January 22, 1980, CEI followed the Uniform System of Accounts and received no recovery

of its expenses in planning and engineering these units. But for the accounting procedures imposed by the Ohio Administrative Code, these expenditures could have been included in test year cost of service and recognized in rates in Appellant's two rate cases between 1973 and 1978. (PUCO Case Nos. 74-571-Y and 78-677-EL AIR).

If the units had been completed and had entered rate base, the dedicated capital investment (including the planning and engineering expenses here under discussion) would then have been recovered, over the property's life, through depreciation accruals. Ohio Revised Code § 4905.18 guarantees to the investor in utility property the recovery of *at least* the original cost of the investment by depreciation accruals. The investor is also allowed an opportunity to earn a return *on* such capital investment after it goes into service, since it becomes part of the utility's rate base. *See* Ohio Revised Code § 4909.15(A)(3); Uniform System of Accounts, 18 CFR 101, Definitions, ¶ 11, at p. 289, and Account No. 403, Depreciation Expense, at p. 314. Stated another way, the investor is not only entitled to get his original money back, but also to have an opportunity to earn a "profit" on his unrecovered investment. *Bluefield Water Works v. Pub. Serv. Comm.*, 262 U.S. 679, 690 (1923).

When CEI prudently and reasonably determined that the four planned generating units should be cancelled, the same Uniform System of Accounts provided for recovery of prudent expenditures through rates as part of Account 182, Extraordinary Property Losses, with the approval of FERC, which was obtained. Since the projects were not completed, the investment could not be allowed in rate base as part of Account 101, Plant in Service. Since the units had never been included in rate base, no depreciation accruals had been recovered through rates. *See Washington Gas Light Co. v. Baker*, 188 F.2d 11 (D.C. Cir. 1950) *cert. den.* 340 U.S. 952 (1951).

The invested dollars, none of which had been recovered in current 'cost of service' in prior rate cases, were required to be moved to Account 182, Extraordinary Property Losses, when the units were, prudently cancelled:

> "A. When authorized or directed by the Commission, this account *shall include extraordinary losses on property abandoned* or otherwise retired from service *which are not provided for by* the accumulated provisions for *depreciation* or amortization and which could not reasonably have been foreseen and provided for, and extraordinary losses, such as unforeseen damages to property, which could not reasonably have been anticipated and which are not covered by insurance or other provisions." (18 CFR 101, at p. 324, Account 182, Extraordinary property losses, emphasis added).

This provision was included in the Uniform System of Accounts when it was originally adopted by the FPC in 1973. *See* 18 CFR 101 (January 1, 1937, at page 103, then Account No. 101.141). This provision was part of the Uniform System of Accounts in 1961 when it was adopted by the Public Utilities Commission of Ohio (18 CFR 101, June 7, 1960, at page 5018) into the Ohio Administrative Code and has remained unchanged to this day. (18 CFR 101, Acct. 182, April 1, 1982, at p. 377).

Indeed, Account 182, "Extraordinary property losses" has been a part of Ohio law for so long, and is so obviously applicable to the circumstances presented here, that the Ohio Court even went so far as to distinguish the Ohio "statutes" in question from the Ohio Administrative Code containing Account 182, "Extraordinary property losses":

> "The *statutes* in question contain no provisions insulating investors from the type of *losses* sustained in the cancelled plants venture." (67 Ohio St.2d at 167, emphasis added.)

In other words, the Ohio Court did not disturb the Commission's finding that CEI's "extraordinary loss" should be accounted for pursuant to Account 182, but merely held that the *statutes* (Ohio Revised Code Sections 4905.22 and 4909.15(A)(4)), as distinguished from the Ohio Administrative Code, did not contain the "extraordinary loss" wording. However, the Ohio statutes do not define "cost," as does the Uniform System of Accounts. Further, the Ohio Administrative Code, containing Account 182, was and is just as binding on CEI as the statutes, and CEI was entitled to rely on its continued applicability when it deferred recovery of its investments from 1973 through 1979 in these generating plants.

The Ohio Court had previously relied upon the accounting rules contained in this very same Uniform System of Accounts in sustaining administrative orders of the Commission. *See Consumers' Counsel v. Pub. Util. Comm. (C&SOE),* 58 Ohio St.2d 108, at 112, 388 N.E.2d 1370 (1979). Indeed, the Ohio Court has previously relied upon these principles of accounting to sustain the Commission's administrative construction of the "cost of service" language in Ohio Revised Code § 4909.15(A)(4), at issue here, to allow the "amortization of deferred scrubber costs" as part of test year expenses under Section 4909.15(A)(4). *See Consumers' Counsel v. Pub. Util. Comm. (C&SOE), supra,* at 116. Further, the Ohio Court had expressly described a utility's "accounting treatment" under the Uniform System of Accounts as "highly probative" of the proper ratemaking treatment for the dedicated capital. *Consumers' Counsel v. Pub. Util. Comm. (Toledo Edison),* 58 Ohio St.2d, 449, 455-456, 391 N.E.2d 311 (1979).

Ohio Revised Code, Section 4909.15, states, in pertinent part, as follows:

> "(A) The public utilities commission, when fixing and determining just and reasonable rates, fares, tolls, and charges shall determine:
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> • • •
>
> (4) The *cost* to the utility *of* rendering the public utility *service* for the test period . . . ." (emphasis added).

The Ohio Court held for the first time in *Consumers' Counsel,* contrary to the provisions of the Uniform System of Accounts, that the words "cost . . . of . . . service" in this statute prohibit the Commission from including in cost of service any cost other than "normal, recurring expenses incurred by utilities in the course of rendering service to the public for the test period." (67 Ohio St.2d at 164).

Thus, Ohio Revised Code § 4905.22 requires a public utility to dedicate its capital to the planning and engineering of future generating plants, the Uniform System of Accounts prohibits the current recovery of those expenditures, and Ohio Revised Code § 4909.15(A)(4), as construed in *Consumers' Counsel,* prohibits the Commission from providing for recovery *of* those same expenditures[15] as costs of service in rates. Appellant submits that is a confiscation of its property without due process of law in violation of the Fifth and Fourteenth Amendments.

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[15]CEI did not propose, and the Commission did not allow, earnings *on* this investment. There is no return or, in layman's terms, "profit", involved at all in this case. In many other cases, commissions have allowed considerably *more* relief to the utility by allowing rate base treatment of the unamortized portion of the cancellation costs. *See Rochester Gas & Elec. Co.,* Case No. 27794, New York Pub. Serv. Comm. Opinion No. 82-1 (January 12, 1982); *Wisconsin Elec. Pwr. Co.,* 40 PUR 4th 630, 688 (1981); *Carolina Power & Light Co.,* No. E-2, Sub 391, North Carolina Pub. Util. Comm. (May 9, 1980).

This Court decades ago held that rates fixed so low as not to cover the "reasonable *cost* of maintaining the road" were confiscatory. *Covington and Lexington Turnpike Road Co. v. Sanford,* 164 U.S. 578, 595 (1896). Likewise, Justice Brandeis, in his classic dissent in *Missouri ex. rel. Southwestern Bell Tel. Co. v. Pub. Serv. Comm.,* 262 U.S. 276 (1923) said that:

> "the compensation which the Constitution guarantees an opportunity to earn is the reasonable *cost* of conducting the business. Cost includes *not only operating expenses, but also capital charges.* Capital charges cover the allowance, by way of interest, for the use of the capital, whatever the nature of the security issued therefor; the allowance for risk incurred; and enough more to attract capital . . . . But a rate is constitutionally compensatory, if it allows to the utility the opportunity to earn the *cost of service* as thus defined." (262 U.S. at 291, emphasis added).

Justice Brandeis advocated "adoption of the amount prudently invested as the rate base and the amount of the capital charge as the measure of the rate of return . . . ." 262 U.S. at 306.

In *Bluefield Water Works Co. v. Public Service Commission of West Virginia,* 262 U.S. 679 (1923), this Court addressed the requirements of the United States Constitution regarding the required rate of return on investment by a utility:

> "A public utility is entitled to such rates as will permit it to earn a return *on* the value of the property which it employs for the convenience of the public equal to that generally being made at the same time, and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures." (262 U.S. at 692-693, emphasis added).

The following year in *Pacific Gas & Electric Co. v. City and County of San Francisco*, 265 U.S. 403 (1924), this Court held that it was unconstitutional confiscation for the District Court to employ in cost of service the reduced costs to manufacture gas made possible by new inventions but to exclude from the valuation of the rate base both 1) the proper valuation for the patented inventions and 2) "recompense for the obsolence" of the utility property which had to be abandoned. (265 U.S. at 415).[16]

The importance of *Pacific Gas* here is that this Court placed particular emphasis on the facts that 1) the patents which rendered the old gas plant obsolete "were of recent conception," 2) the utility could not have provided for the obsolescence of the old plant through depreciation charges in previous rates, and 3) the obsolescence "could not have been long anticipated." The same is true of CEI's investment in these plants.

The denial of at least recovery *of* those costs by Ohio Revised Code § 4909.15(A)(4) as construed and applied to CEI here amounts to the same kind of confiscation as was found unconstitutional in *Pacific Gas, supra.*

Just as the West Virginia Commission in *Bluefield* was not permitted, consistently with the U.S. Constitution, to utilize an artificially low *valuation* of the utility's *rate base* property in arriving at the amount of a fair and reasonable return, so the State of Ohio in this case cannot, by statutory mandate or otherwise, utilize an artificially low determination of CEI's *cost of service* in setting the net return allowable to CEI, if such return,

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[16]Obviously, we do not face precisely the same rate base issue here, since CAPCO's four planned generating units never became part of the rate base. Conversely, in the present case we need not face any issue as to whether depreciation accruals on the "abandoned plant" were sufficient to cover the risk of abandonment, since the expenses involved here were never subject to depreciation accruals.

net of the actual costs incurred by CEI, would not be fair and reasonable under *Bluefield* and like decisions of the Supreme Court of the United States.

This proposition must be obvious. As the Circuit Court of Appeals for the District of Columbia said in reviewing a Federal Power Commission rate order on the issue of the allocation of expenses between jurisdictions:

> "Expenses (using that term in its broad sense to include not only operating expenses but depreciation and taxes) are facts. They are to be ascertained, not created, by the regulatory authorities. *If properly incurred, they must be allowed* as part of the composition of the rates. *Otherwise, the so-called allowance of a return upon the investment, being an amount over and above expenses, would be a farce.*"

*Mississippi River Fuel Corp. v. Fed. Pwr. Comm.*, 163 F.2d 433, at 437 (1947) (emphasis added).

In light of the Ohio Court's announcement of "new law" in its construction of the words "cost . . . of . . . service" in Ohio Revised Code § 4909.15(A)(4), which the Commission was compelled to follow, CEI respectfully submits that Ohio Revised Code § 4909.15(A)(4), as so construed, and as applied in this case, requires the imposition of unconstitutional rates that, in the words of *Bluefield*, "are confiscatory and therefore beyond legislative power." 262 U.S. at 690.

## II. OHIO REVISED CODE § 4905.22 AND § 4909.15 (A)(4), AS CONSTRUED BELOW, DIRECTLY CONFLICT WITH THIS COURT'S DECISION IN *FEDERAL POWER COMMISSION V. HOPE NATURAL GAS CO.*, 320 U.S. 591 (1944).

Ohio Revised Code § 4909.15(A)(4) and § 4905.22, as construed, unconstitutionally exclude prudent planning expenses incurred for the convenience of the public from a utility's allowable cost of service for ratemaking pur-

poses, where the risk of such exclusion was not considered in setting the fair rate of return, thereby unconstitutionally reducing the utility's effective overall net rate of return below the level expressly found to be fair, just, and reasonable.

In *Hope, supra,* this Court upheld the use of an original cost/prudent investment "rate base" as constitutional, emphasizing that the overall objective in ratemaking is not the method employed, but the maintenance of the integrity of the utility's investment. This Court emphasized that basing depreciation expense on original cost assured that ". . . the utility is *made whole* and the integrity of its investment is maintained." (302 U.S. at 606). Thus, the test applied by this Court in evaluating whether the 'result reached' was constitutional was twofold: 1) whether the utility was "made whole," in terms of net investment, and 2) whether the "integrity of its investment" was maintained.[17]

This Court also recognized that the "financial integrity of the company" required "enough revenue not only for *operating expenses* but also for the capital costs of the business. These include service on the debt and dividends on the stock." (320 U.S. at 603). This Court summarized the elements required to meet the just and reasonable test of the Natural Gas Act and to avoid confiscation:

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[17]Ohio Revised Code § 4905.18 guarantees to the investor, through depreciation expense, that he will at least be "made whole" for his capital investment in property which enters rate base. Plainly the Ohio Legislature recognized its constitutional obligation to maintain the integrity of the utility's investment and to make the utility whole where the investment enters rate base and is depreciated. The Commission's initial order allowing amortization in this case, and Account 182 of the Uniform System of Accounts, simply accomplished the same constitutional result where the investment did not become part of the statutory rate base.

> "Rates which enable the company to operate successfully, to maintain its financial integrity, to attract capital, and *to compensate its investors for the risks assumed* certainly cannot be condemned as invalid, even though they might produce only a meager return on the so-called "fair value" rate base." (320 U.S. at 605, emphasis added).

The criteria announced in *Hope* are the criteria for measuring confiscation in violation of the Fifth Amendment. *Permian Basin Area Rate Cases*, 390 U.S. 747, 770 (1968). The confiscation clause of the Fifth Amendment is applicable to the states through the due process clause of the Fourteenth Amendment. *Webb's Fabulous Pharmacies, Inc. v. Bechwith*, 449 U.S. 155, 160 (1980), citing *Chicago, B & Q. R. Co. v. Chicago*, 166 U.S. 226, 239 (1897) and *Penn Central Transportation Co. v. New York City*, 438 U.S. 104, 122 (1978).

Applying these criteria to this case shows clearly that Ohio Revised Code § 4909.15(A)(4), as construed by the Ohio Court and applied by the Commission, confiscates CEI's property. CEI's capital was expended for the convenience of the public pursuant to CEI's statutory obligation to plan and engineer its utility system to serve adequately in the future. CEI's shareholders had not been compensated through depreciation accrual rates nor through rate of return in prior cases for the risk that these planning expenses would be totally excluded from cost of service for ratemaking purposes.

The Court of Appeals for the District of Columbia has had occasion to address a closely analogous situation. In *Washington Gas Light Co., et al. v. Baker*, 188 F.2d 11 (D.C. Cir. 1950), *cert. den.* 340 U.S. 952 (1951), that Court affirmed the District Court's reversal of a Utilities Commission rate order which included the depreciated original cost of the utility's abandoned West Plant *in rate base* in determining the rates. By including the aban-

doned gas plant in rate base, the Commission in *Washington Gas Light* had awarded a return *on* the investment in the abandoned plant. (The issue on this appeal, the recovery *of* the investment in the abandoned gas plant, was not even debated.) The Circuit Court found that the record before the Commission was inadequate for it to determinate whether the investor had *already* received a return *on* the investment for the risk of obsolescence through either 1) depreciation expense in cost of service or 2) "as a risk considered in fixing the permissible rate of return." (188 F.2d at 20). Accordingly, the decision of the Commission was vacated and remanded because it potentially had allowed the investor a return *on* his investment twice. The Circuit Court commented that it seemed "likely . . . in view of the prevalence in the past of the doctrine that abandoned property would not be included in the rate base . . . that investors have been compensated for the risk of obsolescence." (188 F.2d at 20).

In the present case, the investors were *not* compensated through depreciation expense, since there were no depreciation expenses. The four units never got beyond the planning and engineering stage and, therefore, were never accorded a depreciation expense allowance.

Second, CEI's investors were *not* compensated, in fixing the permissible rate of return, for the risk that these planning, engineering, and initial construction costs would be entirely excluded from cost of service.[18] The

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[18] *Washington Gas Light* involved the question of recovery *on* rate base, which was not requested or granted to CEI here. Appellant only requested recovery *of* expenditures in cost of service. It is noteworthy that the Circuit Court *Washington Gas Light* affirmed the Commission's allowance of a recovery *of* rate base investment, by a ten year amortization in cost of service, of 'extraordinary" expenditures for converting customer's appliances from manufactured to natural gas. The "extraordinary" conversion expenditures are obviously closely analogous to the planning expenditures in this case.

reason is precisely the opposite of the facts mentioned by the Circuit Court in *Washington Gas Light*. In *Consumers' Counsel*, the Ohio Court admitted that "the overwhelming weight of authority from other jurisdictions supports the position of the [Ohio] commission" allowing recovery of such planning costs.[19] (67 Ohio St.2d at 162). Since "the overwhelming weight of authority from other jurisdictions" allowed recovery of similar expenses, the investor did *not* anticipate the risk of exclusion from cost of service in Ohio and therefore did *not* cause the market to reflect that risk in a higher required rate of return. The evidence so showed and the Ohio Court's holding that *Consumers' Counsel* announced "new law" confirms that this risk was not anticipated by the investor and was not included in the rate of return allowed in prior rate cases.

In PUCO Case No. 79-537-EL-AIR and PUCO Case No. 80-376-EL-AIR, the fair rate of return allowed *assumed* inclusion in cost of service of these expenses for ratemaking purposes. The Commission initially included these expenses in the allowable cost of service and established both the rate of return and the amount of the total rate increase on that basis. That is, the return allowed was allowed *over and above* recovery of these expenses. In the case on appeal, the Commission simply deducted these expenses from the rates previously allowed, without any

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[19]Copies of unreported decisions and citations to reported decisions from FERC and 22 states were provided to the Ohio Court and were not challenged by the Ohio Court or any party. The citations are included in the Table of Authorities to this Jurisdictional Statement. Although 23 jurisdictions have allowed amortization very recently, there is nothing new about the legal principle. Cases from 16 states dating back to 1929 were cited to the Ohio Court and are also listed in the Table of Authorities.

consideration of CEI's return requirement in *that*[21] situation. Thus, as construed by the Ohio Court, Ohio Revised Code § 4909.15(A)(4) prohibits the Commission from setting rates which "compensate [Appellant's] investors for the risks assumed. . . ." *Hope, supra,* at 605.

The inevitable effect of construing Ohio Revised Code § 4909.15(A)(4) to preclude CEI from recovering such prudent planning expenditures as part of its cost of service is to reduce CEI's effective overall net rate of return on its property employed for the convenience of the public below a level which is fair, just, and reasonable under the *Bluefield* and *Hope* standard. As construed by the Ohio Court in *Consumers' Counsel,* Ohio Revised Code § 4909.15(A)(4) required the Commission to exclude prudent planning expenditures incurred by a utility even though such expenditures would clearly be regarded as legitimate costs of business if incurred by a nonregulated business concern and would be recovered in the price of its product or service. As a consequence, what might otherwise be a fair and reasonable net return, where such planning costs are included, becomes unconstitutionally unfair and unreasonable when the utility has incurred such prudent expenditures, which, as in this case, may be quite large in magnitude, but is not permitted to include such costs before determining the net return on its investment.

Since the investor was not compensated either through depreciation expense or through rate of return, the reasoning of *Washington Gas Light* clearly demonstrates that Ohio Revised Code § 4909.15(A)(4), as construed, simply

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[21]The Commission has subsequently concluded, in CEI's 1981 Case, that the Ohio Court's decision caused an increase in the cost of capital to CEI and, hence, required an increase in the allowed return. *This fact was ignored in the COI case, here on appeal.*

confiscates the capital which CEI was required by law to dedicate to the present and future convenience of the ratepayers.

## CONCLUSION

In its decision in *Consumers' Counsel*, the Ohio Court construed Ohio Revised Code § 4909.15(A)(4) to require the Commission to remove from cost of service the accumulated costs of planning the four cancelled units. The Commission has now removed from cost of service these prudent expenses even though, as it found, it had not in past rates compensated the investor by recognizing a higher overall rate of return as reasonable in light of such a new and unforeseen degree of risk. We are confronted with no evidentiary or technical rate making issues. The facts are not in dispute.

The Commission in Case No. 80-376-EL-AIR allowed amortization of the planning costs as an allowable expense for ratemaking purposes and *then* found a fair and reasonable overall rate of return to be 11.76 percent. The Ohio Court then held in *Consumers' Counsel* that Ohio Revised Code § 4909.15(A)(4) prohibits "the return of capital invested" for such planning and engineering as an allowable expense. The Commission, in its COI order, has now reduced CEI's rates by removing the amount attributable to the cancelled facilities *without considering or revising CEI's revenues, expenses, or rate of return.* As a consequence, the rates have been established based on a cost of service which is artificially low, and the resulting rates inevitably yield an overall rate of return which *must* be below that which has been *found* to be fair, just and reasonable. Such rates, Appellant submits, are confiscatory in violation of the United States Constitution.

For the foregoing reasons, this Court should reverse the decisions of the Ohio Court and allow amortization of Appellant's prudent planning and engineering expenses in its cost of service.

Respectfully submitted,

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**EXHIBIT I**

## OHIO ELECTRIC RATE CASES
## OF
## THE CLEVELAND ELECTRIC ILLUMINATING COMPANY

| 79-537-EL-AIR | 80-376-EL-AIR | 81-1096-EL-COI | 81-146-EL-AIR |
|---|---|---|---|
| Case Noticed 6/19/79 | | | |
| PUCO Hearings 4/2/80-5/22/80 | Case Noticed 4/2/80 | | |
| PUCO *Opinion and Order* 7/10/80 | | | |
| Rates Take Effect 7/14/80 | | | |
| PUCO Rehearing Order 9/3/80 | | | |
| Ohio S.Ct. Appeal Filed 10/22/80 | | | |
| | | | Case Noticed 1/30/81 |
| | PUCO Hearings 3/6/81-4/2/81 | | |
| Ohio S.Ct. Oral Argument 3/26/81 | PUCO *Opinion and Order* 5/4/81 | | |
| | Rates Take Effect 5/6/81 | | |
| | PUCO Rehearing Order 6/24/81 | | |
| Ohio S.Ct. Decision 7/15/81 | | | |
| | Ohio S.Ct. Appeal Filed 8/21/81* | | |
| Ohio S.Ct. Rehearing Order 9/1/81** | | | |

*Cancelled plants issue not appealed by any party.

**Dismissed with standard form Journal Entry without opinion.

**EXHIBIT I (continued)**

## OHIO ELECTRIC RATE CASES
## OF
## THE CLEVELAND ELECTRIC ILLUMINATING COMPANY

| 79-537-EL-AIR | 80-376-EL-AIR | 81-1096-EL-COI | 81-146-EL-AIR |
|---|---|---|---|
| U.S. S.Ct. Appeal Filed 9/2/81 | | | |
| Ohio S.Ct. Motion For Stay Denied** 9/11/82 | | Case Noticed 9/16/81 | |
| | | PUCO Oral Argument 10/13/81 | |
| | | PUCO *Opinion and Order* 10/21/81 | |
| | | Rates Take Effect 10/28/81 | |
| | Ohio S.Ct. Argument 12/1/81 | | |
| | | PUCO Rehearing Order 12/9/81 | |
| | | | PUCO Hearings 12/17/81-2/1/82 |
| | | Ohio S.Ct. Appeal Filed 1/27/82 | |
| U.S. S.Ct. Decision 2/25/82 | Ohio S.Ct. Decision 3/3/82 | | |
| | | | PUCO *Opinion and Order* 3/17/82 |
| | | | Rates Take Effect 3/19/82 |
| | | | PUCO Rehearing Order 5/12/82 |
| | | Ohio S.Ct. Oral Argument (None) | |
| | | Ohio S.Ct. Decision 7/7/82** | |
| | | | Ohio S.Ct. Appeal Filed 7/12/82 |
| | | Ohio S.Ct. Rehearing Order 7/29/82** | |
| | | U.S. S.Ct. Appeal Filed 10/15/82 | |

*Cancelled plants issue not appealed by any party.

**Dismissed with standard form Journal Entry without opinion.

82-704

Case No. .....

Office - Supreme Court, U.S.
FILED
OCT 25 1982
ALEXANDER L. STEVAS,
CLERK

# In the Supreme Court of the United States

**October Term, 1982**

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THE CLEVELAND ELECTRIC ILLUMINATING COMPANY,

*Appellant,*

vs.

THE PUBLIC UTILITIES COMMISSION OF OHIO,

and

OFFICE OF CONSUMERS' COUNSEL,

*Appellees.*

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ON APPEAL FROM THE SUPREME COURT OF OHIO

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## APPENDIX

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*Of Counsel:*

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| Journal Entry and Mandate of Ohio Supreme Court Dismissing Appeal in Case No. 82-165 (filed July 7, 1982) | C-1 |
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| Rehearing Entry of the Public Utilities Commission in Case No. 79-537-EL-AIR (filed September 3, 1980) | I-1 |
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| Ohio Statutes: Ohio Revised Code §§ 4905.13, 4905.18, 4905.20, 4905.22, 4909.15; Ohio Administrative Code § 4901:1-9-05 | K-1 |

**APPENDIX A**

FILED
OCT 15 1982
SUPREME COURT OF OHIO
THOMAS L. STARTZMAN, Clerk

# IN THE SUPREME COURT OF OHIO

**CASE NO. 82-165**

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THE CLEVELAND ELECTRIC
ILLUMINATING COMPANY,
*Appellant,*

v.

THE PUBLIC UTILITIES COMMISSION OF OHIO,

and

OFFICE OF CONSUMERS' COUNSEL,
*Appellees.*

---

**Appeal From the Public Utilities Commission of Ohio**
**Case No. 81-1096-EL-COI**
**In the Matter of the Investigation of the Rates of**
**The Cleveland Electric Illuminating Company.**

---

## NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

---

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*Attorneys for Appellant, The Cleveland Electric Illuminating Company*

# IN THE SUPREME COURT OF OHIO
**CASE NO. 82-165**

THE CLEVELAND ELECTRIC
ILLUMINATING COMPANY,
*Appellant,*

v.

THE PUBLIC UTILITIES COMMISSION OF OHIO,

and

OFFICE OF CONSUMERS' COUNSEL,
*Appellees.*

**Appeal From the Public Utilities Commission of Ohio**
**Case No. 81-1096-EL-COI**
**In the Matter of the Investigation of the Rates of**
**The Cleveland Electric Illuminating Company.**

## NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

Notice is hereby given that The Cleveland Electric Illuminating Company, Appellant before the Ohio Supreme Court, hereby appeals to the Supreme Court of the United States from the final judgment of the Supreme Court of the State of Ohio entered into these proceedings on July 7, 1982, rehearing having been denied on July 29, 1982, which granted the motion to dismiss Appellant's appeal filed by the Office of Consumers' Counsel, thereby affirming the October 21, 1981 *Opinion and Order* of the Public Utilities Commission of Ohio in Case No. 81-1096-EL-COI.

This appeal is taken pursuant to 28 U.S.C. § 1257(2).

*Of Counsel:*

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*Attorneys for The Cleveland Electric Illuminating Company*

## CERTIFICATE OF SERVICE

I hereby certify that true copies of the foregoing Notice of Appeal were served on all parties of record by United States Mail, first-class, postage prepaid, to their last known addresses, this 15th day of October, 1982, as follows:

WILLIAM J. BROWN,
*Ohio Attorney General*
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ALAN P. BUCHMANN,
*Counsel of Record for Appellant,*
The Cleveland Electric Illuminating Company

## APPENDIX B

# THE SUPREME COURT OF THE STATE OF OHIO

THE STATE OF OHIO, }
CITY OF COLUMBUS. } 1982 Term
To wit: July 29, 1982

CLEVELAND ELECTRIC ILLUMINATING CO.,
*Appellant*,
vs.
PUBLIC UTILITIES COMMISSION OF OHIO,
*Appellee*.

**No. 82-165**
**REHEARING**

It is ordered by the court that rehearing in this case is denied.

I, THOMAS L. STARTZMAN, Clerk of the Supreme Court of the State of Ohio, do hereby certify that the foregoing entry was correctly copied from the records of said Court, to wit, from Journal No. ..... Page .....

IN WITNESS WHEREOF, I have hereunto subscribed my name and affixed the seal of the Supreme Court this 29th day of July, 1982.

THOMAS L. STARTZMAN,
*Clerk*.

By _____,
*Deputy*.

## APPENDIX C

# THE SUPREME COURT OF THE STATE OF OHIO

| | |
|---|---|
| THE STATE OF OHIO,<br>CITY OF COLUMBUS. | 1982 Term<br>To wit: July 7, 1982 |
| CLEVELAND ELECTRIC ILLUMINATING CO.,<br>*Appellant,*<br>vs.<br>PUBLIC UTILITIES COMMISSION OF OHIO,<br>*Appellee.* | **No. 82-165<br>APPEAL<br>FROM THE<br>PUBLIC UTILITIES<br>COMMISSION<br>OF OHIO<br>ON MOTION<br>TO DISMISS** |

This cause, here on appeal from the PUBLIC UTILITIES COMMISSION, was heard in the manner prescribed by law. On consideration thereof, the motion to dismiss is sustained and cause dismissed.

It is ordered that a mandate issue to the PUBLIC UTILITIES COMMISSION OF OHIO to carry this judgment into execution.

I, THOMAS L. STARTZMAN, Clerk of the Supreme Court of Ohio, certify that the foregoing entry was correctly copied from the Journal of this Court.

Witness my hand and the seal of the Court this ____ day of _____, 19____.

_____*Clerk*

_____*Deputy*

# THE SUPREME COURT OF THE STATE OF OHIO

THE STATE OF OHIO,
CITY OF COLUMBUS.

1982 Term
To wit: July 7, 1982

CLEVELAND ELECTRIC ILLUMINATING CO.,
*Appellant,*
vs.
PUBLIC UTILITIES COMMISSION OF OHIO,
*Appellee.*

**No. 82-165**
**MANDATE**

To the Honorable PUBLIC UTILITIES COMMISSION OF OHIO, Within and for the County of Franklin, Ohio, Greeting:

The Supreme Court of Ohio commands you to proceed without delay to carry the following judgment in this cause into execution:

Motion to dismiss sustained and appeal dismissed.

THOMAS STARTZMAN,
*Clerk*

....., 19....

.....*Deputy*

**RECORD OF COSTS**

Docket Fee ..... $20.00 Paid by Squire, Sanders & Dempsey

## APPENDIX D

## BEFORE

## THE PUBLIC UTILITIES COMMISSION OF OHIO

| | |
|---|---|
| IN THE MATTER OF THE INVESTIGATION OF THE RATES OF THE CLEVELAND ELECTRIC ILLUMINATING COMPANY. | Case No. 81-1096-EL-COI |

### ENTRY ON REHEARING

The Commission, coming now to consider the above-entitled matter, and specifically its Opinion and Order in this case issued October 21, 1981, the application for rehearing filed by the Cleveland Electric Illuminating Company (CEI) on November 18, 1981, and the memorandum contra filed by the Office of Consumers' Counsel (OCC) on November 30, 1981, hereby issues the following entry on rehearing.

**Commission Review and Discussion**

In the two most recent rate proceedings involving CEI, Case No. 79-537-EL-AIR, Opinion and Order July 10, 1980 and Case No. 80-376-EL-AIR, Opinion and Order May 4, 1981, we have included in CEI's allowable test year expenses the amortization of CEI's share of the costs associated with the cancellation of four nuclear plants. On appeal of the decision in Case No. 79-537-EL-AIR, the Ohio Supreme Court found that the inclusion of those costs was unreasonable and unlawful. *Consumers' Counsel v. Public Utilities Commission*, 67 Ohio St. 2d 153 (1981). In order to implement the directives of the Supreme Court in that decision we initiated this investigation, pursuant to Section 4905.26, Revised Code, and by Order dated Oc-

tober 21, 1981, directed CEI to remove these costs from its current rates.

On November 18, 1981 CEI filed an application for rehearing setting forth nine areas of alleged error. OCC filed a memorandum contra on November 30, 1981. In part, CEI contends that these proceedings were initiated, conducted and determined without authority of law. In addition, CEI claims that it was improper for this hearing to be conducted without the taking of evidence, and that such procedure has deprived CEI of its statutory and constitutional rights. The company also submits that the Commission deviated from prior Ohio law by eliminating a single item from expenses without taking into consideration all aspects of the company's current condition. In sum, CEI contends:

> [t]he said Opinion and Order, by its failure to recognize and allow recovery of prudent expenditures made in the interest of providing public service and as mandated by statute, contravenes the public policy of the State of Ohio, unlawfully imperils the future rendition of reliable utility service, unlawfully deprives respondent of its property, and unreasonably impinges on the financial security of all Ohio utilities and hence upon the cost and reliability of utility service rendered to Ohio consumers. (Application p. 4)

We are not unmindful of the position taken by CEI and the uniqueness of the situation that is before us. However, we believe that the intent of the Supreme Court was that positive steps be taken to grant CEI consumers rate relief as a result of its decision. As we stated previously in our Opinion and Order, we are of the opinion that the best method of implementing the intent of the Supreme Court's decision in *Consumers' Counsel v. Public Utilities Commission, supra,* is the method we have chosen. In light of that decision, the objections raised by CEI must be overruled and rehearing denied.

It is, therefore,

ORDERED, That the rehearing application filed November 18, 1981 by The Cleveland Electric Illuminating Company be denied. It is, further,

ORDERED, That copies of this Entry on Rehearing be served on all parties of record.

THE PUBLIC UTILITIES
COMMISSION OF OHIO

/s/ JOHN KELLY
(Chairman)

/s/ DENNIS PINES

/s/ MICHAEL DELBANE
(Commissioners)

Entered in the Journal

December 9, 1981

A True Copy

DAVID M. POLK

David M. Polk
Secretary

# APPENDIX E

## BEFORE

## THE PUBLIC UTILITIES COMMISSION OF OHIO

| | |
|---|---|
| IN THE MATTER OF THE INVESTIGATION OF THE RATES OF THE CLEVELAND ELECTRIC ILLUMINATING COMPANY. | Case No. 81-1096-EL-COI |

## OPINION AND ORDER

The Commission, coming now to consider the above-entitled matter, having reviewed the arguments introduced at public hearing and the briefs of the parties, and being fully advised of the facts and issues in this case, hereby issues its Opinion and Order.

**Appearances:**

Mr. Alan D. Wright, General Counsel, and Mr. Craig I. Smith, Senior Counsel, 55 Public Square, Cleveland, Ohio, and Messrs. Squire, Sanders & Dempsey, by Mr. Alan P. Buchmann, 1800 Union Commerce Building, Cleveland, Ohio, on behalf of the Applicant, The Cleveland Electric Illuminating Company.

Mr. William J. Brown, Attorney General of Ohio, by Mr. Marvin I. Resnik, Mrs. Marsha Rockey Schermer and Mr. Jonathan L. Heller, Assistant Attorneys General, 375 South High Street, Columbus, Ohio, on behalf of the Staff of the Public Utilities Commission of Ohio.

Mr. William A. Spratley, Consumers' Counsel, by Ms. Gretchen J. Hummel, Mr. Martin J. Marz and Mr. Steven M. Sherman, Associate Consumers' Counsel, 137 East State Street, Columbus, Ohio, on behalf of the residential customers of The Cleveland Electric Illuminating Company.

Mr. Thomas E. Wagner, Director of Law, and Mr. Craig Glazer, Assistant Director of Law, Cleveland City Hall, 601 Lakeside Avenue, Cleveland, Ohio, on behalf of the City of Cleveland, Ohio.

Messrs. Bell & Clevenger, L.P.A., by Messrs. Langdon D. Bell and Samuel C. Randazzo, 21 East State Street, Columbus, Ohio, on behalf of the Industrial Electricity Consumers.

**History of the Proceedings:**

In its Opinion and Order of July 10, 1980 in Case No. 79-537-EL-AIR, and in the May 4, 1981 Opinion and Order in Case No. 80-376-EL-AIR, the last two rate proceedings involving The Cleveland Electric Illuminating Company (CEI), the Commission authorized the inclusion in allowable expenses of the amortization of CEI's share of the costs associated with the cancellation of four nuclear plants. On appeal of the decision in Case No. 79-537-EL-AIR, the Ohio Supreme Court found that the inclusion of those costs was unreasonable and unlawful. *Consumers' Counsel v. Public Utilities Commission,* 67 Ohio St. 2d 153 (1981). In light of that decision, the Commission initiated this investigation of CEI's rates, pursuant to Section 4905.26, Revised Code, by Entry dated September 16, 1981.

The decision of the Supreme Court of Ohio in *Consumers' Counsel v. Public Utilities Commission, supra,* was reported on July 19, 1981. Issuance of the Court's mandate, however, was stayed, pursuant to Supreme Court Rule IX, Section 2, by the filing of an application for rehearing by CEI. The application for rehearing was denied by Supreme Court Entry dated September 1, 1981, and the Court issued its mandate. Promptly, CEI filed a motion for a stay of the mandate which was denied by the Supreme Court of Ohio on September 11, 1981. On September 2, 1981, CEI filed with the Supreme Court of Ohio a notice of appeal to the United States Supreme Court and

on September 22, 1981, CEI applied to the United States Supreme Court for a stay of the execution of the mandate of the Ohio Supreme Court. The application for a stay to the United States Supreme Court was denied on October 13, 1981.

Pursuant to the Commission Entry of September 16, 1981 a prehearing conference was held in this matter on September 23, 1981. At that time it was decided that briefs would be submitted by the parties and that the hearing scheduled for October 13, 1981 would be limited to oral argument on the briefs. The hearing was conducted on October 13, 1981 and the record certified to this Commission for appropriate action.

The parties hereto are The Cleveland Electric Illuminating Company (CEI or Company), the Office of the Consumers' Counsel (OCC), the City of Cleveland (City) and the Industrial Electric Consumers (IEC), the latter three having been granted leave to intervene by entry or ruling at the hearing held on October 13, 1981. A petition to intervene filed by Senior Citizens, et al. was denied by the attorney examiner by entry of October 8, 1981, and no appeal to the Commission has been taken.

**Commission Review and Discussion:**

The issue before the Commission at this time is the selection of an appropriate method for implementing the mandate issued by the Supreme Court of Ohio on September 1, 1981. This issue is clouded, however, by complexities that are beyond the control of this Commission or any of the parties appearing before it. The mandate issued by the Supreme Court of Ohio was issued in Commission Case No. 79-537-EL-AIR, Opinion and Order issued July 10, 1979. The rates for electric service authorized and established in Case No. 79-537-EL-AIR were found to be unreasonable and, therefore were, supplanted by those rates established by the Commission in Case No. 80-376-EL-AIR, Opinion and Order issued May 4, 1981. In Case

No. 80-376-EL-AIR the Commission also allowed the annual amortization of the costs associated with the cancelled nuclear plants as part of operating expenses for rate making purposes. No appeals from that aspect of the Commission's decision are pending.[1] In addition, the Company has another rate case pending in Case No. 81-146-EL-AIR, based upon a more current test year, which should commence hearings in late 1981 or early 1982. Thus, although the mandate issued by the Court is clear in its intent, the intent of the Court as to how it is to be implemented may not be.

As noted, the Commission could implement the Court's decision in one of several ways. First of all it could conduct an investigation of the rates established in Case No. 79-537-EL-AIR, although clearly this would be a meaningless exercise. The Commission could simply reduce the rates currently in effect by virtue of Case No. 80-376-EL-AIR by an amount equal to the amortization adjustment; this would ignore, however, all other changes in circumstance that have occurred since the implementation of those rates. Or the Commission could apply the mandate of the Supreme Court on a prospective basis in Case No. 81-146-EL-AIR, which will commence hearings in a few months. The Commission, however, has chosen to implement the Supreme Court's mandate through the initiation of this proceeding. We believe that this is the best method to effectuate the Supreme Court's mandate in the most expedient fashion.

The Office of Consumers' Counsel (OCC) and the City of Cleveland both contend that the remand of the Supreme Court of Ohio requires that this Commission immediately redetermine CEI's allowable operating ex-

[1] It should be noted that intervenor Senior Citizens, et al., noticed an appeal, which appeal is presently pending, which did raise the issue of the lawfulness of the inclusion of the amortization in allowable expenses. By letter dated September 3, 1981, Senior Citizens, et al., notified the Court that it would not pursue that issue.

penses excluding therefrom the expenditures attributable to the cancelled nuclear facilities and reduce CEI's current rates accordingly. OCC and the City of Cleveland contend that the order of the Supreme Court was specifically directed to a single issue and that changes that may have taken place in other items since the establishment of these rates need not be considered. The City of Cleveland and OCC contend that the adjustment can be made on the data available to the Commission in the most recent rate proceeding. In essence, these parties contend that this Commission should apply the remand of Case No. 79-537-EL-AIR to Case No. 80-376-EL-AIR in a simplistic fashion. The problem, of course, is that CEI's present rates were fixed not in Case No. 79-537-EL-AIR, but in Case No. 80-376-EL-AIR, and there is no remand or mandate in the latter.

The Company contends that the rates established in Case No. 80-376-EL-AIR are presumptively just and reasonable pursuant to Section 4909.15, Revised Code, and the Supreme Court's decision in the prior rate case does not change this presumption. The Company contends that the decision of the Supreme Court should not result in an automatic adjustment of previously-established rates.

In the alternative, the Company contends that if the Supreme Court decision is deemed a sufficient basis for the institution of an investigation into the current rates, such an investigation must consider more than a single item subtracted from the Company's allowable expenses. The Company points out that the test period in Case No. 80-376-EL-AIR was the calendar year 1980, and that we are currently through most of 1981 and a great number of the circumstances have changed. The Company contends that in order to make a determination that CEI's rates should be reduced, this Commission must consider more than the one expense item dealt with by the Supreme Court. The Company points out that the theories behind rate making and the test year concept do not provide for

an item by item guaranteed dollar-for-dollar recovery, but rather the establishment of a reasonable allowance for a normal and necessary utility function. The Company argues that although the Supreme Court has stated that the abandonment loss can no longer be considered in establishing this "reasonable allowance", it does not necessarily follow that it must be removed from a reasonable allowance established in the past, without considering all of the elements that make up that allowance.

A further complicating factor is that we are not concerned solely with the inclusion in rates of this expense, but with the impact of the disallowance of the same, requiring careful consideration of all of the implications of such disallowance on the accumulated deferred balances being amortized. Some of those implications were discussed in the Commission's Opinion in Case No. 79-537-EL-AIR and their significance was indicated in Ohio Edison, Case No. 81-898-EL-AEM. The potential influence on the cost of capital and the financial standing of CEI should not be overlooked.

The Commission, thus, is confronted with a series of involved and inter-related problems. In the first instance, it cannot meaningfully act directly on the remand, because the remand is in a case which has since been superseded. Similarly, we must reject OCC's request (OCC Brief p. 5) that we calculate CEI's allowable expenses "based upon the test year data in the remand proceeding," which is the 1979 data while CEI's present rates are based on a 1980 test year. On the other hand, CEI's argument that we must, in effect, conduct a new rate case now seems impracticable in view of the fact that hearings should be conducted in the relatively near future in Case No. 81-146-EL-AIR in which the adequacy of CEI's present rates may be fully explored. The Commission does not mean to say that it is appropriate or, even for that matter, lawful, generally speaking, to adjust rates by a single item because of events occurring after its decision nor, conversely, that

the technical status of a case or series of cases should be employed to promote form over substance. We believe that a practicable solution is required and that the basic thrust of the Ohio Supreme Court's decision in *Consumers' Counsel v. Public Utilities Commission, supra,* can be implemented in these circumstances, while preserving the legal rights of the utility. In a sense, the fact that the rates set in Case No. 79-537-EL-AIR have been superseded in Case No. 80-376-EL-AIR is, as a practical matter, counterbalanced by the fact that rates set in Case No. 80-376-EL-AIR will, presumably, soon be superseded in Case No. 81-146-EL-AIR.

The Commission concludes, therefore, that CEI should be directed to file tariffs which reduce its present rates. The Commission is mindful, however, that CEI's appeal to the United States Supreme Court is still pending and that CEI has stated that it intends to pursue that appeal vigorously. In order to obviate any future questions with respect to the amount foregoing through this rate reduction, therefore, CEI is authorized and directed to maintain the same in the appropriate deferred reserves. Such reserves, including this presently foregone amortization, should be maintained by CEI pending a final decision on the lawfulness of the inclusion of these costs in allowable expenses for rate-making purposes or such action as the Commission may take after a full review of all aspects of this question in CEI's pending electric rate case. Obviously, if CEI should eventually prevail on its appeal to the United States Supreme Court, this will do no more than temporarily postpone the recovery of these costs while, in the meantime, CEI consumers will receive the present rate relief which we believe the Ohio Supreme Court expected and which the intervening parties have requested. The Commission will also be able in the context of a full rate case, to consider all of the implications of the Ohio Supreme Court's decision and take such pertinent action as it may deem appropriate.

**ORDER:**

It is, therefore,

ORDERED, That The Cleveland Electric Illuminating Company submit tariffs for the approval of this Commission, reducing its present rates by an amount equal to the revenue requirements attributable to the cancelled nuclear facilities included therein. It is, further,

ORDERED, That The Cleveland Electric Illuminating Company submit three (3) complete copies of the tariffs by October 26, 1981, to be reviewed by the Commission and approved by subsequent entry. It is, further,

ORDERED, That The Cleveland Electric Illuminating Company continue to defer the accumulated amounts, including the amounts which would have been amortized but for this rate reduction, on its books, as part of the presently accrued deferred reserves with respect to such costs, pending further direction from this Commission and that, at the time it submits the tariffs required by the preceding paragraph of this order, it submit to the Commission's accounting staff the details of the accounting procedures by which it intends to maintain such deferral. It is, further,

ORDERED, That a copy of this Opinion and Order be served on all parties of record in this proceeding.

THE PUBLIC UTILITIES COMMISSION OF OHIO

/s/ JOHN KELLY
(Chairman)
DENNIS PINES
MICHAEL DELBANE
(Commissioners)

Entered in the Journal
Oct. 21, 1981

A True Copy
DAVID M. POLK

David M. Polk
Secretary

## APPENDIX F

THE STATE OF OHIO, } 1982 Term
CITY OF COLUMBUS. } To wit: September 11, 1981

Office of Consumers' Counsel
Senior Citizens Coalition et al.,
City of Cleveland,
Appellants

vs.

Public Utilities Commission
of Ohio,
Appellees.

No. 80-1480
No. 80-1528
No. 80-1547

Upon consideration of the motion for stay of execution of mandate, it is ordered by the court that this motion be, and the same hereby is, denied.

I, THOMAS L. STARTZMAN, Clerk of the Supreme Court of the State of Ohio, do hereby certify that the foregoing entry was correctly copied from the records of said Court, to wit, from Journal No. _____ Page _____.

IN WITNESS WHEREOF, I have hereunto subscribed my name and affixed the seal of the Supreme Court this _____ day of _____, 19 _____.

_____
Clerk.

By _____,
Deputy.

## APPENDIX G-1

## DECISIONS OF THE SUPREME COURT OF OHIO DENYING REHEARING

**(Filed September 1, 1981)**

# THE SUPREME COURT OF THE STATE OF OHIO

THE STATE OF OHIO,
CITY OF COLUMBUS.

1981 Term
To wit: September 1, 1981

CITY OF CLEVELAND,
*Appellant,*

vs.

PUBLIC UTILITIES COMMISSION OF OHIO et al.,
*Appellees.*

No. 80-1547
REHEARING

It is ordered by the court that rehearing in this case is denied.

I, THOMAS L. STARTZMAN, Clerk of the Supreme Court of the State of Ohio, do hereby certify that the foregoing entry was correctly copied from the records of said Court, to wit, from Journal No. .... Page ....

IN WITNESS WHEREOF, I have hereunto subscribed my name and affixed the seal of the Supreme Court this 1st day of September, 1981.

THOMAS L. STARTZMAN,
*Clerk.*

By ----------,
*Deputy.*

## APPENDIX G-2

## DECISIONS OF THE SUPREME COURT OF OHIO DENYING REHEARING

**(Filed September 1, 1981)**

# THE SUPREME COURT OF THE STATE OF OHIO

THE STATE OF OHIO,
CITY OF COLUMBUS.
} 1981 Term
To wit: September 1, 1981

SENIOR CITIZENS COALITION et al.,
*Appellants,*
vs.
PUBLIC UTILITIES COMMISSION OF OHIO et al.,
*Appellees.*
} No. 80-1528 REHEARING

It is ordered by the court that rehearing in this case is denied.

I, THOMAS L. STARTZMAN, Clerk of the Supreme Court of the State of Ohio, do hereby certify that the foregoing entry was correctly copied from the records of said Court, to wit, from Journal No. .... Page ....

IN WITNESS WHEREOF, I have hereunto subscribed my name and affixed the seal of the Supreme Court this 1st day of September, 1981.

THOMAS L. STARTZMAN,
*Clerk.*

By ----------,
*Deputy.*

## APPENDIX G-3

## DECISIONS OF THE SUPREME COURT OF OHIO DENYING REHEARING

**(Filed September 1, 1981)**

# THE SUPREME COURT OF THE STATE OF OHIO

THE STATE OF OHIO, City of Columbus. } 1981 Term To wit: September 1, 1981

OFFICE OF CONSUMERS' COUNSEL, *Appellant*, vs. PUBLIC UTILITIES COMMISSION OF OHIO et al., *Appellees*. } No. 80-1480 REHEARING

It is ordered by the court that rehearing in this case is denied.

I, THOMAS L. STARTZMAN, Clerk of the Supreme Court of the State of Ohio, do hereby certify that the foregoing entry was correctly copied from the records of said Court, to wit, from Journal No. ___ Page ___.

IN WITNESS WHEREOF, I have hereunto subscribed my name and affixed the seal of the Supreme Court this 1st day of September, 1981.

THOMAS L. STARTZMAN,
*Clerk.*

By _____,
*Deputy.*

# APPENDIX H

## DECISION AND OPINION OF THE SUPREME COURT OF OHIO

**(Filed July 15, 1981)**

**Statement of the Case.**

OFFICE OF CONSUMERS' COUNSEL, APPELLANT, *v.*
PUBLIC UTILITIES COMMISSION OF OHIO ET AL., APPELLEES.

SENIOR CITIZENS COALITION ET AL., APPELLANTS, *v.*
PUBLIC UTILITIES COMMISSION OF OHIO ET AL., APPELLEES.

CITY OF CLEVELAND, APPELLANT, *v.*
PUBLIC UTILITIES COMMISSION OF OHIO ET AL., APPELLEES.

[Cite as Consumers' Counsel v. Pub. Util. Comm. (1981), 67 Ohio St. 2d 153.]

*Public Utilities Commission—Electric companies—Rate increase—Allowable operating expenses—Amortization of cost of terminated nuclear facilities, unlawful.*

The Public Utilities Commission's treatment of a utility's investment in terminated nuclear generating stations as amortizable costs to be recovered from the utility's ratepayers is inconsistent with the ratemaking formula contained in R. C. 4909.15 and is unreasonable and unlawful.

(Nos. 80-1480, 80-1528 & 80-1547—
Decided July 15, 1981.)

APPEALS from the Public Utilities Commission of Ohio.

These three cases are appeals taken from an order of appellee, Public Utilities Commission of Ohio (hereinafter "commission"), granting intervening appellee, the Cleveland Electric Illuminating Company (hereinafter "CEI"), a rate increase of approximately $69.6 million. The commis-

Statement of the Case.

sion order further provided for the amortization over a ten-year period of CEI's substantial investment in four terminated nuclear power plants.[1]

The commission's order dealt with two cases that had been consolidated. Case No. 79-537-EL-AIR involved CEI's application to increase rates. Case No. 79-744-EL-CMR concerned a complaint and appeal taken by CEI from a 1979 rate setting ordinance passed by the City of Cleveland.

Inasmuch as these three appeals primarily concern issues relating to the nuclear power plant cancellations, we shall briefly reprise the history of these now terminated facilities. In 1967, CEI joined with four other electric companies to form the Central Area Power Coordination Group (CAPCO).[2] The CAPCO companies sought to achieve economies of scale and greater service reliability by jointly planning, constructing, and operating electrical generating facilities. In 1973, the CAPCO group committed itself to build the four nuclear plants at issue herein based on forecasts that predicted a substantially increased demand for electricity by the CAPCO companies' customers during the 1970's and 1980's. These forecasts subsequently had to be revised downward when increasing energy costs spurred conservation efforts and significantly softened the demand for electricity. Moreover, the 1979 accident at Three Mile Island prompted the Nuclear Regulatory Commission to issue stringent and costly new standards for nuclear power plants, requiring major design changes in the Babcock and Wilcox units that CAPCO planned to construct and oper-

[1] Davis-Besse Units 2 and 3 and Erie Units 1 and 2 are the cancelled facilities at issue.

[2] In addition to CEI the CAPCO group consists of Toledo Edison, Ohio Edison, and two Pennsylvania utilities, Duquesne Light Co. and Pennsylvania Power Co.

**Statement of the Case.**

ate. After much study and redesign the CAPCO companies decided to terminate the four units on January 23, 1980. When the decision to cancel the plants was announced, CAPCO had already invested considerable sums in the projects. Preliminary expenses included expenditures for engineering, siting, environmental, geological, and seismic studies, and for obtaining state and federal licenses. Moreover, to comply with detailed regulatory requirements and complete all the necessary documents, certain plant components had to be purchased at a fairly early stage in the planning process. CEI's share of the total CAPCO investments in the four cancelled plants amounted to approximately $56,400,000 as of the date of termination.

The instant CEI rate case was pending before the commission when the plant terminations were announced.[3] The commission had accepted CEI's application for a rate increase as of September 17, 1979, and had established calendar year 1979 as the test year and June 30, 1979, as the date certain. The commission staff conducted an investigation and issued its initial report in March 1980. This report did not make reference to the terminated nuclear plants because CEI did not officially inform the commission of the plant cancellations until February 1980. The commission staff, at appellants' request, then conducted a supplemental investigation to consider the effect of the terminated plant expenditures on CEI's rate application. The staff completed its investigation of the cancelled nuclear facilities and filed revised schedules in mid-April. The staff recommended that the investment in the four nuclear plants should be amortized over a ten-year period as CEI had requested.

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[3] The rates established by the commission order in the instant ratemaking case have recently been superseded by new rates set by order on May 4, 1981 in case No. 80-376-EL-AIR.

**H-4**
**Consumers' Counsel v. Pub. Util. Comm.**
**67 Ohio St. 2d 153 (1981)**

**Opinion, per SWEENEY, J.**

Public hearings on the rate increase application began on April 2, 1980, and continued for 32 days. Staff witnesses appeared and testified at the hearings in regard to the cancelled nuclear plants and other matters contained in the application. Appellants were represented at, and participated fully in, these public hearings.

The commission issued its order on July 10, 1980. Appellants timely filed for a rehearing which the commission denied as to the issues raised in the present appeal.

These causes are now before this court upon appeals as of right.

*Mr. William A. Spratley,* consumers' counsel, *Mr. Gary M. Petroff* and *Ms. Gretchen J. Hummel,* for appellant Consumers' Counsel.

*Mr. Joseph P. Meissner,* for appellants Senior Citizens Coalition *et al.*

*Mr. Thomas E. Wagner,* director of law, and *Mr. Craig A. Glazer,* for appellent City of Cleveland.

*Mr. William J. Brown,* attorney general, *Mr. Marvin I. Resnik* and *Mr. David M. Neubauer,* for appellee Public Utilities Commission.

*Mr. Alan D. Wright, Mr. Craig I. Smith, Messrs. Squire, Sanders & Dempsey, Mr. Alan P. Buchmann, Mr. Lowell L. Garrett, Mr. William C. Donahue* and *Mr. Richard W. McLaren, Jr.,* for intervenor-appellee The Cleveland Electric Illuminating Co.

SWEENEY, J. The scope of this court's review of commission orders is set forth in R. C. 4903.13, which states in pertinent part:

"A final order made by the public utilities commission shall be reversed, vacated, or modified by the supreme court on appeal, if, upon consideration of the record, such

court is of the opinion that such order was unlawful or unreasonable."

"Under the 'unlawful or unreasonable' standard specified in R. C. 4903.13, this court will not reverse or modify an opinion and order of the Public Utilities Commission where the record contains sufficient probative evidence to show that the commission's determination is not manifestly against the weight of the evidence and is not so clearly unsupported by the record as to show misapprehension, mistake or willful disregard of duty," *Columbus v. Pub. Util. Comm.* (1979), 58 Ohio St. 2d 103, 104. See, also, *Consumers' Counsel v. Pub. Util. Comm.* (1979), 58 Ohio St. 2d 108, 110; *Ohio Utilities Co. v. Pub. Util. Comm.* (1979), 58 Ohio St. 2d 153, 164; *Duff v. Pub. Util. Comm.* (1978), 56 Ohio St. 2d 367, 370; *General Motors Corp. v. Pub. Util. Comm.* (1976), 47 Ohio St. 2d 58, paragraph two of the syllabus; *Cleveland Electric Illuminating Co. v. Pub. Util. Comm.* (1975), 42 Ohio St. 2d 403, paragraph eight of the syllabus. We assess the appellants' objections with this standard of review in mind.

I A.

In its order the commission allowed approximately $91 million to be included in the rate base for construction work in progress (CWIP) pursuant to R. C. 4909.15(A)(1) and 4909.15(E). R. C. 4909.15(A)(1) states in relevant part:

"* * *The commission may, in its discretion, permit a reasonable allowance for construction work in progress but, in no event, may any allowance for construction work in progress be made by the commission until it is determined, after a physical inspection, that the particular construction project is a least seventy-five per cent complete."

R. C. 4909.15(E) imposes the following limitation on allowable CWIP:

Opinion, per SWEENEY, J.

"In no event shall an allowance for construction work in progress under division (A)(1) of this section exceed twenty per cent of the total valuation as stated in such division, not including such allowance."

Some $90 million of the CWIP allowance was directly attributable to the Bruce Mansfield coal-fired generating station, which came on line several months after the new rates became effective. It is unquestioned that Bruce Mansfield met the 75 percent completion criterion for rate base eligibility pursuant to R. C. 4909.15(A)(1). Moreover, it is uncontroverted that inclusion of the Bruce Mansfield-related CWIP did not exceed the 20 percent of total valuation limitation imposed by R. C. 4909.15(E).

I A(i).

Appellants Senior Citizens Coalition et al. (hereinafter "SCC"), in case No. 80-1528, challenge the commission's allowance for CWIP in this case on the basis that the CWIP provisions contained in R. C. 4909.15(A)(1) represent an unconstitutional delegation of legislative power. Specifically, SCC contends that the statute "***establishes no definite policy nor provides any standard for the exercise of PUCO discretion in permitting an allowance for construction work in progress and***therefore the PUCO should be prohibited from granting any such allowance.***"

We find no merit in SCC's constitutional challenge to the CWIP provisions because the commission's discretion is sufficiently circumscribed by the specific eligibility criteria enumerated in the statute. As we stated in *Consumers' Counsel v. Pub. Util. Comm., supra* (58 Ohio St. 2d 108), at page 113:

"***We believe these limitations adequately confine commission discretion. Further restriction would conceivably hinder the flexibility necessary to enable the com-

mission to carry out legislative will. For these reasons, this court holds that the discretion granted the commission under R. C. 4909.15 to authorize a reasonable allowance for construction work in progress in a utility's rate base constitutes a lawful delegation of the state's police power by the General Assembly."

We expressed the same view of the CWIP provisions of R. C. 4909.15(A)(1) in *Cleveland v. Public Util. Comm.* (1980), 63 Ohio St. 2d 62, 68. In the case at bar we decline to strike down the CWIP statute as an unconstitutional delegation of legislative authority.

I A(ii)

Both SCC and appellant City of Cleveland, in case No. 80-1547, contend that the inclusion of a CWIP allowance in this case constituted an abuse of commission discretion. As previously noted, the Bruce Mansfield generating station, which accounted for virtually all of the CWIP at issue, met the 75 percent completion criterion and came on line several months after the new rates went into effect. Under these circumstances, we cannot say that the commission's decision was either manifestly against the weight of the evidence or unsupported by the record. *Columbus vs. Pub. Util. Comm., supra.* Therefore, we refuse to disturb the commission's findings on the propriety of including a CWIP allowance in CEI's rate base. Accordingly, we reject appellants' assertions that the commission abused its discretion in granting the CWIP allowance.

II.

SCC alleges that the commission did not adequately investigate CEI's generating capacity to determine whether the utility had excess capacity. The commission staff investigated CEI's generating capacity and determined that

the reserve capacity was adequate but not excessive.[4] Staff and CEI witnesses testified to the same effect at the hearings before the commission wherein they explained the methodology by which they reached their conclusions.

We have in a previous case acknowledged the difficulties the commission and utilities face on the excess capacity issue.

"***Since utilities must anticipate load growth years in advance to maintain adequate capacity to ensure reliable service, it is unrealistic to expect a utility to have only the precise amount of capacity needed at a given time." *Cleveland v. Pub. Util. Comm., supra*, at 65. To paraphrase what we stated in *Consumers' Counsel v. Pub. Util. Comm.* (1980), 64 Ohio St. 2d 71, 79: Limited judicial review of an excess capacity determination is sound for the reason that while excess capacity analyses have an aura of precision about them, they are fraught with judgments and assumptions. Given the inherent problems of accurately projecting load growth, we are satisfied that the commission's excess capacity methodology is reasonable and that the factual findings are supported by the record. SCC's challenge on the question of excess capacity is, therefore, without merit.

III A.

Before proceeding to the merits of appellants' contentions on the question of whether the commission lawfully and reasonably treated the four cancelled nuclear power plants as amortizable costs, we must first consider two procedural issues raised by appellant Cleveland in case No. 80-1547. Cleveland first contends that CEI violated the

[4] The record indicates that CEI had available 3,469 megawatts (MW) of capacity. The 1979 peak load was 3,097 MW and the forecasted 1980 peak load was 3,450 MW.

notice provisions of R. C. 4909.18 and 4909.19, R. C. 4909.18(E) requires that "[a] proposed notice for newspaper publication fully disclosing the substance of the application" must accompany the rate increase application. R. C. 4909.19 requires the applicant to publish in newspapers of general circulation the "substance and prayer of its application."[5] Cleveland asserts that CEI's proposed notice under R. C. 4909.18 and its published notice under R. C. 4909.19 were inadequate because no mention was made of the four terminated nuclear units in either notice.

Cleveland relies on *Committee Against MRT v. Pub. Util. Comm.* (1977), 52 Ohio St. 2d 231, and *Ohio Assn. of Realtors v. Pub. Util. Comm.* (1978), 60 Ohio St. 2d 172, to support its contention that CEI's statutory notices were inadequate. In *MRT, supra,* we stated, at page 233, that "***a highly innovative and material change in the *method of charging* customers should be included in the notice." (Emphasis added.) The cancelled power plant information that Cleveland insists should have been included in the CEI notices herein complained of did not relate to an innovative method of charging that would profoundly affect the rates paid by certain categories of utility customers. Therefore, Cleveland's reliance on *MRT* and *Realtors* is misplaced.

The proposed notice under R. C. 4909.18(E) need only convey the "substance" of the application and the notice published pursuant to R.C. 4909.19 need only contain the "substance and prayer" of the application. The decision of the CAPCO companies to terminate the pro-

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[5] Appellees challenge Cleveland's standing to complain of the allegedly flawed notices. The standing question, however, was not raised before the commission and, therefore, according to our well-settled rule, the issue is not properly before this court. *Stores Realty Co. v. Cleveland* (1975), 41 Ohio St. 2d 41, 43.

posed plants did not alter the "substance" or the "substance and prayer" of CEI's application because CEI did not request additional rate relief when it revised its original application to reflect the terminated plant expenditures. We hold that the CEI notices met the standards of R. C. 4909.18 and 4909.19, and consequently Cleveland's assertions to the contrary are unfounded.

III B.

Cleveland's second procedural objection relates to the adequacy of the staff investigation and report in regard to the cancelled nuclear power plants. R. C. 4909.19 requires that the commission investigate and issue a report on rate increase applications. The commission did conduct an investigation and prepared a report on the original CEI application. As noted however, the initial commission staff report was silent on the subject of the terminated plants because the decision to cancel the plants was announced too late to be included in the report. However, the staff did subsequently investigate the matter of the terminated facilities and assessed the effect of the cancelled generating stations on CEI's pending rate application. Cleveland now complains that the omission of these matters from the original report and the tardy presentation of the staff review of the four terminated plants after hearings on the application had already begun were prejudicial and in violation of R. C. 4909.19. Cleveland asserts that "intervenors have been consistently denied the opportunity to adequately prepare their case. They have [had] no opportunity to review the Staff's findings prior to hearings and thus no opportunity to prepare evidence to support or rebut the same."

**Opinion, per SWEENEY, J.**

Notwithstanding these contentions, Cleveland, after posing objections to the original report, did receive the benefits of the staff's investigation of the four terminated nuclear plants and had ample opportunity to cross-examine the commission's and CEI's experts at the public hearings. Cleveland did not seek additional time to prepare its case while these matters were pending before the commission. Moreover, Cleveland had already intervened in the case before the plant closing issue surfaced and therefore was not prejudiced by the omission of the cancelled plant data in the original report. *Worthington Hills Civic Assn. v. Pub. Util. Comm.* (1976), 45 Ohio St. 2d 11.

The purpose of the staff report is "***to facilitate meaningful contest of rate increase applications by providing interested parties with the materials necessary for an informed challenge." *Duff v. Pub. Util. Comm.* (1978), 56 Ohio St. 2d 367, 376. The commission report in this case, as supplemented by the follow-up investigation conducted by the commission staff, provided appellant Cleveland with the opportunity to make an informed challenge. Therefore, the commission's investigation and report in the instant rate application case comply with the statutory requirements set forth in R. C. 4909.19.

IV A.

The core issue in each of these appeals is whether the commission lawfully and reasonably permitted CEI to treat its investment in the four cancelled nuclear generating stations as amortizable costs.

The commission order stated and analyzed the question in this fashion.

"***What the company seeks is the recovery of costs incurred on behalf of its ratepayers to assure that adequate service could be maintained***. The significant question,

given the Commission's past pronouncements with respect to the impropriety of the recovery of past losses through future rates, is whether the amortization of these extraordinary costs does violence to this principle. The distinguishing feature that sets this adjustment apart from those we have rejected on this ground in the past is that costs associated with the termination of the units did not really become costs until the fact of termination. Cancellation does not create a past loss, but gives rise to a current cost.***[R]ejection of this adjustment would have a very direct impact on applicant's final performance as, in the absence of funding of the amortization through rates, applicant would be required to write off these costs currently***. Thus, we now see the wisdom of the standard emerging from the cases from other jurisdictions; if the expenditures are prudent, amortization should be permitted.

"In determining whether these expenditures were prudent, one must bear in mind what is and what is not at issue. No one disputes that the 1973 decision to embark on the construction in question was reasonable as it was based on the best data available***. Similarly, no one disputes that the decision to terminate construction was reasonable, given the intervening decline in growth expectations and the uncertainties which now attend the construction of nuclear units.*** The Commission finds that applicant's decisions were reasonable and prudent at every step of this process, and concludes that the proposed adjustment should be approved."

The appellants argue that the commission exceeded its authority and disregarded a carefully crafted statutory scheme when it acceded to CEI's request to amortize the cancelled nuclear plant expenditures.

There is no question but that the overwhelming weight of authority from other jurisdictions supports the

position of the commission.[6] In only two instances has amortization been disallowed.[7] It is important to note, however, that none of the previous rulings on this precise issue represents the opinion of the highest court of the jurisdiction in which the case arose. Virtually all of the decisions that the commission, CEI, and the *amici* cite in support of amortization derive from regulatory proceedings. Even more significant is the fact that no other case has considered the propriety of the commission's proposed amortization with reference to Ohio law. Thus, while counsel for the parties and intervenors before the court in this cause have thoroughly canvassed the administrative decisions in other jurisdictions and have supplied this court with copies of those decisions, we must regard these foreign regulatory opinions as advisory in nature. The construction of Ohio law is particularly the province of this court, and we are nowise bound by the pronouncements of regulatory regimes elsewhere in effect.

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[6] See, *e.g.*, *Re San Diego Gas & Electric Co.* (Cal. Pub. Util. Comm. 1979), 29 P.U.R. 4th 613; *Re Potomac Electric Power Co.* (Md. Pub. Ser. Comm. 1977), Order No. 6999; *Re Consumer Power Co.* (Mich. Pub. Ser. Comm. 1975), Case No. F-700; *Re Northern States Power Co.* (Minn. Pub. Ser. Comm. 1977), Dkt. E-0021 GR-76-934; *Re Public Service Electric and Gas Co.* (N.J. Dept. of Energy, Bd. of Pub. Util. 1980), Dkt. No. 794-310; *Re Consolidated Edison Co. of New York* (N.Y. Pub. Ser. Comm. ), Case No. 9187; *Re Carolina Power & Light Co.* (N.C. Util. Comm. 1979), Dkt. No. E-2, Sub. 352; *Re Gulf States Utilities Co.* (Pub. Util. Comm. of Texas 1979), Dkt. No. 2677; *Re Virginia Electric & Power Co.* (Va. Corp. Comm. 1979), 29 P.U.R. 4th 65; *Re Wisconsin Electric Power Co.* (Pub. Ser. Comm. of Wis. 1980), Case No. 05-C1-3; *Re Potomac Electric Power Co.* (D.C. Pub. Ser. Comm. 1979), 29 P.U.R. 4th 517.

[7] See *Re Arizona Public Service Co.* (Ariz. Corp. Comm. 1980), Decision No. 51009; *Re Northern States Power Co.* (Pub. Ser. Comm. of N.D. 1980), Case No. 10,097.

Opinion, per SWEENEY, J.

IV B.

The commission's approval of amortization was predicated on the prudence of CEI's original decision to build the nuclear facilities and the subsequent decision to cancel the plants. We must decide whether the test of prudence, as applied by the commission, which supports treating the expenditures associated with the terminated nuclear generating stations as amortizable costs, is consistent with the statutorily mandated ratemaking formula contained in R. C. 4909.15.

IV B(i).

The controversy surrounding the cancelled nuclear power plants focuses primarily on R. C. 4909.15(A)(4), which delineates the service-related costs that a utility may recover from its ratepayers. This section states in relevant part:

"The public utilities commission, when fixing and determining just and reasonable rates, fares, tolls, rentals, and charges shall determine:

"***

"(4) The cost to the utility of rendering the public utility service for the test period***"

The commission urges that "an expenditure by a utility can be considered a cost of rendering the public utility service if it fails in fact to achieve its intended purpose*** [if] the expense was reasonably calculated to provide [future] utility service at a reasonable cost." The underpinnings for the commission rationale may be found in those statutory provisions that require utilities to maintain adequate service presently and for the foreseeable future. See, *e.g.*, R. C. 4905.22 (adequate service and facilities).

Notwithstanding the provisions that impose a duty on utility companies to plan for the future, the question under

R. C. 4909.15(A)(4) remains whether the cancelled plant expenditures represent "[t]he cost to the utility of rendering the public utility service for the test period." Test period considerations aside, what the company sought and what the commission granted was the amortization as service-related costs of an investment that never provided any service whatsoever to the utility's customers.

We seriously question whether the General Assembly contemplated that the commission would treat the type of expenditures controverted herein as costs under R. C. 4909.15(A)(4). The now terminated nuclear plants represented a major capital investment that ultimately would have been included in the rate base under R. C. 4909.15 (A)(1), had the projects not been cancelled. It is our opinion that R. C. 4909.15(A)(4) is designed to take into account the normal, recurring expenses incurred by utilities in the course of rendering service to the public for the test period.[8] A non-exhaustive list of such expenses would include reasonable expenditures for repairs, maintenance, personnel-related costs, administrative expenses, and taxes.

The extraordinary loss sustained by CEI in connection with the terminated n..clear plants cannot be transformed into an ordinary operating expense pursuant to R. C. 4909.15(A)(4) by commission fiat. The commission's statement that "[c]ancellation does not create a past loss, but gives rise to a current cost" is unpersuasive. Under this rationale we question whether there could ever be a "past loss" the return of which would not be recoverable in future ratemaking proceedings notwithstanding the com-

[8] Appellants contend that the "direct, primary benefit" test enunciated in *Cleveland* v. *Pub. Util. Comm.* (63 Ohio St. 2d 62), *supra*, is applicable to the case at bar. We disagree. The direct, primary benefit standard should not be wrenched from the institutional advertising expenses and charitable contributions context in which it arose.

mission's assertion to the contrary. The commission's characterization of the investment in the four terminated plants as "cost" under R. C. 4909.15(A)(4) in light of what we perceive to be the legislative intention underlying that section is unreasonable. Therefore, to the extent that the commission's order in regard to the cancelled plants is predicated on R. C. 4909.15(A)(4), the order cannot stand.

IV B(ii).

The commission and CEI also argue that even if, as we have found, R. C. 4909.15(A)(4) is inapplicable, then under R. C. 4909.15(D)(2)(b) the commission may authorize the amortization of the investment in the terminated nuclear facilities.

R. C. 4909.15 states in relevant part:

"(D) When the public utilities commission is of the opinion, after hearing and after making the determinations under divisions (A) and (B) of this section***that the maximum rates, charges, tolls, or rentals chargeable by any such public utility are insufficient to yield reasonable compensation for the service rendered, and are unjust and unreasonable, the commission shall:

"***

"(2) With due regard to all such other matters as are proper, according to the facts in each case,

"***

"(b)***fix and determine the just and reasonable rate, fare, charge, toll, rental, or service to be rendered, charged, demanded, exacted, or collected for the performance or rendition of the service that will provide the public utility the allowable gross annual revenues under division (B) of this section, and order such just and reasonable rate, fare, charge, toll, rental, or service to be substituted for the existing one.***"

**Opinion, per SWEENEY, J.**

For purposes of R. C. 4909.15(D)(2)(b) the question presented is whether the cancelled nuclear power plant costs fall under the "all such matters as are proper" language of the statute. The commission views R. C. 4909.15(D)(2)(b) as a virtual wild card to be played whenever the commission in its discretion sees fit. We interpret the statute less sweepingly, first because the provisions are linked inextricably with the ratemaking factors contained in R. C. 4909.15(A) and (B), and secondly because the General Assembly undoubtedly did not intend to build into its recently revised (1976) ratemaking formula a means by which the commission may effortlessly abrogate that very formula.

To be a proper matter giving rise to a permissible adjustment under R. C. 4909.15(D)(2)(b), the matter in question must relate to factors otherwise included in R. C. 4909.15. R. C. 4909.15(D)(2)(b) makes reference to "the allowable *gross* annual revenues under division (B)." (Emphasis added.) Having previously determined that the nuclear plant costs are not properly includable under R. C. 4909.15(A), then these costs can have no effect on the gross annual revenue determination under R. C. 4909.15(B). Therefore, we reject the commission's argument invoking R. C. 4909.15(D)(2)(b) as alternative statutory authority for its order granting CEI permission to amortize its investment in the cancelled nuclear facilities.

It is our view that R. C. 4909.15(D)(2)(b) is designed to allow the commission to make minor adjustments to rates ascertained by the statutory formula when the criteria upon which the rates are based are skewed for one reason or another. Thus, under R. C. 4909.15(D)(2)(b), the commission may smooth out anomalies in the ratemaking equation that tend to make the test year data unrepresentative for ratemaking purposes.

**Opinion, per SWEENEY, J.**

IV B(iii)

"[T]his court has consistently recognized that the Public Utilities Commission is a creature of the General Assembly and may exercise no jurisdiction beyond that conferred by statute." *Dayton Communications Corp. v. Pub. Util. Comm.* (1980), 64 Ohio St. 2d 302, 307. See, also, *Werlin Corp. v. Pub. Util. Comm.* (1978), 53 Ohio St. 2d 76, 80; *Ohio Public Interest Group v. Pub. Util. Comm.* (1975), 43 Ohio St. 2d 175, 176, paragraph five of the syllabus; *Penn Central Transportation Co. v. Pub. Util. Comm.* (1973), 35 Ohio St. 2d 97, paragraph one of the syllabus. Stated differently, the commission may not legislate in its own right. This, however, is what the commission has attempted to accomplish in the case at bar.

The commission order engrafts upon the statutory rate-making scheme an exception that would allow utility companies to recover their investment in unfinished projects ineligible for rate base treatment if the original decision to build the facilities and the subsequent decision to cancel the projects are prudent under the circumstances. In so doing the commission has exceeded its statutory mandate. We hold that the commission unreasonably and unlawfully exceeded its statutory authority when it approved amortization of CEI's investment in the four terminated nuclear power plants.

IV C.

Appellants contend that the commission also erred in including the cancelled plant costs in the calendar year 1979 test period because the termination was not announced until January 23, 1980. Inasmuch as we have already determined that the commission improperly allowed amortization of the utility's investment in the terminated nuclear facilities, it is unnecessary for us to address the timing issue raised in this cause.

**Opinion, per SWEENEY, J.**

IV D.

We are mindful of the policy considerations that prompted the commission's decision. The commission, CEI, and the *amici* argue strenuously that to rule as we have today will seriously disadvantage Ohio utilities in capital markets thereby "driv[ing] up the return on investment required by investors in Ohio utilities." This gloomy scenario, however, does not imbue the commission with the authority to rewrite the statutes. The statutes in question contain no provisions insulating investors from the type of losses sustained in the cancelled-plants venture.

If, as has been argued, these are parlous times for the utilities industry, and if, therefore, in order to attract and retain investment capital, utility companies must not only be granted a fair and reasonable rate of return pursuant to statute but must also be assured the return of capital invested in failed projects that would otherwise not be recoverable under the ratemaking formula, then the commission and the utilities should petition the General Assembly to enact changes in the ratemaking structure so as to provide this extra modicum of protection for the investors. Absent such explicit statutory authorization, however, the commission may not benefit the investors by guaranteeing the full return of their capital at the expense of the ratepayers. Under the ratemaking formula now in effect consumers are not chargeable for utility investments and expenditures that are neither included in the rate base nor properly categorized as costs. What we previously stated in a rate base case is applicable to the case at bar: "***It is only proper that their [the investors] venture be found operational before they commence to recoup their capital outlays from the consumers." *Consumers' Counsel v. Pub. Util. Comm.* (1979), 58 Ohio St. 2d 449, 456-457.

**Opinion, per SWEENEY, J.**

We take a dimmer view of the second policy argument advanced by the commission to support its order. The commission suggests that if the appellants prevail on this issue, then "[r]ather than prudently cancel certain projects, it is not inconceivable that at least some utility managements would complete expenditures on a project and have ratepayers pay a return on dollars which would have more wisely not been spent." R. C. 4909.154 specifically empowers the commission to investigate management policies, practices and organization to determine whether a public utility is properly managed. If a utility completes a project that should have been abandoned, then the commission must under the "used and useful" requirement of R. C. 4909.15(A)(1) disallow rate base treatment and under R. C. 4909.154 disallow any claimed operating expenses related to the unnecessary project. We are confident that if any utility managers who might be tempted to act as the commission suggests are aware that the commission, pursuant to its statutory responsibilities, is vigorously scrutinizing all proposed and in-progress construction projects, these managers will decide whether or not to abandon a particular project according to their best and most prudent business judgment. Thus, we reject the commission's argument that our decision today may engender imprudent decision making in utility company boardrooms.

For reasons hereinbefore stated the order of the commission is affirmed in part and reversed in part, and this cause is remanded to the commission for a redetermination of CEI's allowable operating expenses, excluding therefrom the expenditures attributable to the cancelled nuclear facilities.

*Order reversed in part and affirmed in part.*

**Consumers' Counsel v. Pub. Util. Comm.**
**67 Ohio St. 2d 153 (1981)**

**Concurring and Dissenting Opinion, per P. BROWN, J.**

CELEBREZZE, C. J., W. BROWN and C. BROWN, JJ., concur.

P. BROWN, LOCHER and HOLMES, JJ., concur in part and dissent in part.

PAUL W. BROWN, J., concurring in part and dissenting in part.

I concur in Parts I, II and III of the majority opinion insofar as they affirm the commission's decision to allow rate base treatment for CWIP attributable to the Bruce Mansfield coal-fired generating station. I dissent, however from Part IV of the opinion.

In Part IV of its opinion, the majority reverses the commission's decision to allow amortization of the costs incident to termination of the four nuclear facilities in question. In so doing, the majority does not disturb the commission's findings that CEI acted both prudently and reasonably in incurring these costs. Instead, the majority holds that it was not the intent of the General Assembly to treat expenditures of this type as "costs" within the meaning of R. C. 4909.15(A)(4). I believe the majority's interpretation of this section to be too restrictive.

The term "cost" is not defined in R. C. Chapter 4909. Therefore, it is necessary to look elsewhere to ascertain the meaning of this word. In 1961, the commission adopted standard accounting procedures to be used by Ohio utilities. "The system of accounts and records identified and designated as 'Uniform System of Accounts Prescribed for Public Utilities and Licensees effective January 1, 1961' * * * is adopted by this Commission * * *." Ohio Adm. Code 4901:1-9-05. This "Uniform System of Accounts" was promulgated in 18 C.F.R., Part 101.

An analysis of this uniform system clearly demonstrates that expenditures such as those incurred in the termination of the four nuclear generating units were in-

tended to fall within the statutory definition of "costs." The uniform system states, in part:

"182 Extraordinary property losses.

"A. * * * this account shall include extraordinary losses on property *abandoned* or otherwise retired from service which are not provided for by the accumulated provisions for depreciation or amortization and which could not reasonably have been foreseen and provided for ***." (Emphasis added.) *Id.*, at 324.

"407 Amortization of property losses.

"This account shall be charged with amounts credited to account 182***." *Id.*, at 356.

This accounting system has been in effect in Ohio for approximately two decades. Given this fact, we can reasonably assume that the General Assembly was cognizant of its existence when it amended R. C. 4909.15 in 1976, and that it was not the intent of the General Assembly to treat these extraordinary property losses in a different manner in which they were treated by the Public Utilities Commission.

Moreover, as the majority correctly notes, "the overwhelming weight of authority from other jurisdictions supports the position of the commission." The majority dismisses this significant point with the facile statement that none of the cases from these other jurisdictions represents the opinion of the highest court of the jurisdiction; nor, has any other jurisdiction construed or applied Ohio law in reaching its determination. While I do not assert that decisions from other jurisdictions are controlling in Ohio, I cannot accept the majority's summary disposition of these foreign decisions. First, this court, in the past, has recognized the persuasive value of decisions from other jurisdictions in this area. See *Ohio Water Service Co.* v. *Pub. Util. Comm.* (1980), 64 Ohio St. 2nd 12. Second, the

near unanimity of decisions from other jurisdictions allowing amortization of these types of expenditures further demonstrates the reasonableness of the commission's decision in this case.

Appellants urged before this court that before any expense or cost could be passed on to the ratepayers, it must confer a direct and primary benefit upon said ratepayers. Implicit in the majority's decision is an acceptance of this argument. Thus, the majority, today, takes another step toward entrenching the spurious "direct, primary benefit" test into the public utilities law of Ohio.[9]

"Review of orders of the Public Utilities Commission on appeal is limited to a consideration of whether the order is unreasonable or unlawful***." *Cremean v. Pub. Util. Comm.* (1976), 48 Ohio St. 2d 163, paragraph one of the syllabus. The order in the instant cause is neither unreasonable nor unlawful. Accordingly, I would affirm the decision of the commission in its entirety.

HOLMES, J., concurs in the foregoing concurring and dissenting opinion.

LOCHER, J., concurring in part and dissenting in part. I concur in the syllabus and Parts III (notice and staff investigation) and IV (amortization) of the majority opinion. I would also note, however, that the financial effect of this decision on CEI will be insignificant. CEI informed its investors in its "1979 Annual Report":"*** The Company [CEI] will seek the approval of the Federal Energy Regulatory Commission and The Public Utilities Commission of Ohio for authority to amortize [the costs previously expended toward the four nuclear units whose construction CAPCO terminated] over a suitable number of years. The extent to which these costs may be recovered

[9] See Justice Herbert's dissent in *Cleveland* v. *Pub. Util. Comm.* (1980), 63 Ohio St. 2d 62, 75, in which I concurred.

through rates will be determined by the PUCO. If any costs of termination are not permitted to be recovered, the Company would be required to reduce Net Income by the disallowed amount. In any event, the resolution of these matters should not have a material adverse impact on the financial position of the Company."

I dissent from Part I of the majority opinion (CWIP), because PUCO refuses to define standards for review of CWIP matters. My dissenting opinions in *Consumers' Counsel* v. *Pub. Util. Comm.* (1979), 58 Ohio St. 2d 108, 117, and *Consumers' Counsel* v. *Pub. Util. Comm.* (1981), 66 Ohio St. 2d 162, 167, express the reasons for my concern.

## APPENDIX I

## BEFORE
## THE PUBLIC UTILITIES COMMISSION OF OHIO

| | |
|---|---|
| In the Matter of the Application of The Cleveland Electric Illuminating Company for Authority to Amend and Increase Certain of its Filed Schedules Fixing Rates and Charges for Electric Service. | Case No. 79-537-EL-AIR |
| In the Matter of the Complaint and Appeal of The Cleveland Electric Illuminating Company from Ordinance No. 1673-79 of the Council of the City of Cleveland, Ohio Passed August 7, 1979, entitled "An Ordinance Setting the Maximum Rates which may be Charged by The Cleveland Electric Illuminating Company for Electric Service Within the City of Cleveland." | Case No. 79-774-EL-CMR |

### REHEARING ENTRY

The Commission, coming now to consider the above-entitled matters, and, specifically, its opinion and Orders in these dockets of July 10, 1980, and its applications for rehearing filed by the applicant and other participating parties, hereby makes the following findings.

1) On July 10, 1980, the Commission issued its Opinion and Order in these dockets granting, in part, the application of the Cleveland Electric Illuminating Company for authority to increase its rates and charges for electric service rendered

jurisdictional customers, and sustaining the company's complaint that Ordinance No. 1673-79 of the City of Cleveland was unjust and unreasonable.

2) Rehearing applications were timely filed pursuant to the provisions of Section 4903.10 Revised Code by the applicant, the City of Cleveland, the Office of Consumers' Counsel, Senior Citizens, *et al.*, and the Industrial Electricity Consumers.

3) Through its rehearing application, the Illuminating Company alleges that the Commission's July 10, 1980 Opinion and Order is unreasonable and unlawful in some 39 particulars. Review of these assignments of error indicates that the majority represent nothing more than a restatement of the company's original objections relative to those issues which have now been decided adversely to the applicant. The Commission is of the opinion that these claims were adequately considered in the order now complained of with the exception of three of the issues which the applicant elected to address in the memorandum accompanying its rehearing application.

4) By its twenty-fourth assignment of error, applicant alleges that the Commission unreasonably refused to adjust test-year labor expense to recognize wage increases which became effective subsequent to the test period. In considering this ground for rehearing, the Commission must first point out that adjustments for out-of-period cost changes, while accepted in some instances where strict conditions are satisfied, are the exception rather than the rule. If the test-year concept is to remain a viable basis for determining cost of service, a matching of revenues and expenses must be maintained. The Commission has departed from this principle in only the most compelling circumstances as, for example, in cases where we are confronted with a very remote test

year (*Columbia Gas of Ohio*, Case No. 77-1309-GA-AIR [May 24, 1979]). Applicant argues that the adjustment proposed in this proceeding does satisfy the conditions discussed in prior Commission orders, specifically *East Ohio Gas Company*, Case No. 79-535-GA-AIR (July 9, 1980). As the Commission has granted rehearing on this issue in the *East Ohio* case (*East Ohio Gas Company, supra*, Entry on Rehearing, August 7, 1980) we believe the matter deserving of further consideration in these dockets as well. Rehearing on this ground should be granted.

5) Through the twenty-eighth ground advanced by the company as a basis for rehearing, applicant contends that the Commission erred in excluding certain advertising costs from allowable expenses without evidence as to whether the advertisements in question benefited the customers. As the Commission found in the order now complained of, these advertisements appeared to be solely promotional in character. However, on the day preceeding the issuance of the Opinion and Order, the Supreme Court of Ohio handed down its decision in *Cleveland v. Public Utilities Commission*, 63 Ohio St. 2d 62 (1980), whereby a new test for the eligibility of advertising expenses was apparently established. As the Commission will herein grant the rehearing sought by certain other participants with respect to the advertising question in light of this development, we deem it appropriate to also permit the company to participate in our efforts to interpret the import of the Court's decision. We, therefore, find the application for rehearing on this ground to be well made and hereby grant rehearing on this issue.

6) By its twenty-ninth assignment of error, applicant charges that the Commission acted unreasonably in failing to include any allowance for charitable contributions in the cost of service

determination. In the Commission's view, this result, which was a departure from previous Commission practice, was mandated by the Court's decision in *Cleveland v. Public Utilities Commission*, supra. Applicant argues that the language of the Court's decision will admit of other interpretations, a view which the Commission believes the company should be entitled to pursue through argument and the presentation of additional evidence. Rehearing should be granted for this purpose.

7) Rehearing should be denied with respect to all other grounds set out by applicant.

8) The City of Cleveland charges that the Commission's Opinion and Order of July 10, 1980 is unreasonable and unlawful in a number of particulars. These grounds relating to the issues of the used and useful nature of Davis-Besse, excess capacity, construction work in progress, terminated generating units, rate case expense, legal fees, and tariff matters were all adequately addressed in the Commission's original opinion and no further discussion is necessary. Rehearing on these grounds should be denied. Some response is required, however, to the City of Cleveland's assertion that the Commission could not properly find that the rates contained in Ordinance No. 1653-79 of the City of Cleveland from which the complaint and appeal in Case No. 79-774-EL-CMB was taken were unreasonable.

9) Review of the record clearly indicates that the Commission did allocate property, revenues, and expenses between the ordinance area and the balance of the company's service territory and that it did so based on evidence presented by the staff (S.R., pp. 4-6, 162-163). The fact that the City of Cleveland chose not to inquire of the staff witness on this subject does not mean that these allocations were unsupported. The or-

dinance rates were quite clearly unjust and unreasonable in that they generated revenues which were grossly insufficient to provide the company reasonable compensation for the service rendered affected customers. Further, the City's arguments relative to interclass allocations reveal a basic misapprehension of the class responsibility methodology employed by the company. We commend Applicant's Exhibit Nos. 6, 9 and 1 (Sched. B-6 and Sched. C-4) to the City's attention. Rehearing on this ground should be denied.

10) Consistent with our above discussion, the City of Cleveland's application for rehearing on the issue of advertising expenses should be granted.

11) The Office of Consumers' Counsel assigns as error only the Commission's determination that the costs associated with the termination of four nuclear generating units should be included in the cost of service in these proceedings. No arguments have been advanced which have not adequately been addressed in the Commission's Opinion and Order and rehearing on this ground should be denied.

12) Intervenor Senior Citizens, *et al.*, seeks rehearing on the question of the inclusion of Davis-Besse in rate base, excess capacity, construction work in progress, cash working capital, terminated nuclear units, and certain tariff matters. The Commission is of the opinion that these matters have been adequately discussed in the order now complained of and finds that rehearing on these grounds should be denied. In keeping with our earlier findings, Senior Citizens' application for rehearing with respect to the issue of advertising expense should be granted.

13) The rehearing application filed by the intervening Industrial Electricity Consumers is actually taken from the Commission's Entry of July 14,

1980 in this docket whereby the Commission accepted applicant's new tariffs for filing. Intervenors contend that this Entry contains the erroneous finding that the tariffs, as submitted, conformed to the Commission's July 10, 1980 Opinion and Order. Specifically, intervenors charge that the Industrial and Large Industrial rate schedules approved (PUCO No. 11, 6th Rev. Sheet No. 26 and PUCO No. 11, 6th Rev. Sheet No. 28) are not consistent with the Commission's directive concerning the adjustments to the proposed tariffs necessary to reflect the fact that the revenue increase authorized was somewhat less than that originally requested by the company.

14) In the July 10, 1980 Opinion and Order, the Commission did not specifically set out the method to be employed in adjusting the tariffs. The Commission found only that the staff tariff recommendations which were not subject to specific objection should be implemented. Among those recommendations was the staff suggestion that if the rate relief authorized was less than that requested, the reductions in the various rate schedules should be performed so as to retain the proportionality between the various blocks (S.R., p. 56). The applicant also supported this technique (Tr. XX, pp. 55-56) which, it might be noted, represents the approach customarily followed by the Commission under such circumstances (See *e.g. Dayton Power and Light*, Case No. 79-510-EL-AIR [July 31, 1980]).

15) The Commission agrees with the Industrial Electricity Consumers that the Industrial and Large Industrial rate sheets submitted by the applicant and accepted by the Commission's July 14, 1980 Entry reflected no downward adjustment to the original base energy portions of the rate structures as originally proposed. However, the impact of the failure of the company to adjust all portions of these rates is so slight (actually less than a

fraction of a percent) that the Commission does not believe that the basic proportionality of the rates has been meaningfully altered. The new schedules, as filed, reasonably satisfied the Commission's intent and the Entry approving these schedules should be affirmed. The rehearing application of the intervening Industrial Electricity Consumers should be denied.

It is, therefore,

ORDERED, That the rehearing application filed August 8, 1980, by the Cleveland Electric Illuminating Company be, and hereby is granted to the extent provided above and denied in all other respects. It is, further,

ORDERED, That the rehearing application filed August 11, 1980, by the City of Cleveland be, and hereby is granted to the extent provided above and denied in all other respects. It is, further,

ORDERED, That the rehearing application filed August 8, 1980, by the Office of Consumers' Counsel be, and hereby is denied. It is, further,

ORDERED, That the rehearing application filed August 8, 1980, by Senior Citizens, *et al.*, be, and hereby is granted to the extent provided above and denied in all other respects. It is, further,

ORDERED, That the rehearing application filed August 7, 1980, by the Industrial Electricity Consumers, be and hereby is denied. It is, further,

ORDERED, That the rehearing granted to consider the issues identified above be, and hereby is scheduled to commence at 9:30 A.M. on Wednesday, October 8, 1980, at the offices of the Commission, 375 South High Street, Columbus, Ohio. It is, further,

ORDERED, That copies of this Entry be served upon all parties of record.

THE PUBLIC UTILITIES COMMISSION OF OHIO

/s/ WILLIAM NEWCOMB
(Chairman)

/s/ STEPHEN A. REILLY

/s/ MICHAEL DELBANE
(Commissioners)

Entered in the Journal
Sept. 3, 1980

A True Copy
DAVID M. POLK

David M. Polk
Secretary

# APPENDIX J

## Opinion and Order of the Public Utilities Commission of Ohio

(Filed July 10, 1980)

**BEFORE**

**THE PUBLIC UTILITIES COMMISSION OF OHIO**

| | |
|---|---|
| In the Matter of the Application of The Cleveland Electric Illuminating Company for Authority to Amend and Increase Certain of its Filed Schedules Fixing Rates and Charges for Electric Service. | Case No. 79-537-EL-AIR |
| In the Matter of the Complaint and Appeal of The Cleveland Electric Illuminating Company from Ordinance No. 1673-79 of the Council of the City of Cleveland, Ohio Passed August 7, 1979, entitled "An Ordinance Setting the Maximum Rates which may be Charged by The Cleveland Electric Illuminating Company for Electric Service Within the City of Cleveland". | Case No. 79-774-EL-CMR |

## OPINION AND ORDER

The Commission, coming now to consider the above-entitled permanent rate application filed by the Cleveland Electric Illuminating Company pursuant to Section 4909.18 Revised Code and the above-styled complaint and appeal filed by the Cleveland Electric Illuminating Company pur-

suant to Section 4909.34 Revised Code; the Staff Report of Investigation issued pursuant to Section 4909.19 Revised Code; having appointed its attorney examiner, Barth E. Royer, pursuant to Section 4901.18 Revised Code to conduct a public hearing and to certify the record thereof directly to the Commission; the testimony and exhibits introduced into evidence at the public hearing commencing April 2, 1980, and concluding May 22, 1980; its prior Entries and Orders in these dockets; and being otherwise fully advised in the premises and in compliance with Section 4903.09 Revised Code, hereby issues its Opinion and Order.

**History of the Proceedings:**

The Cleveland Electric Illuminating Company, the applicant herein, is an Ohio corporation engaged in the business of supplying electric service in this state. The company provides retail service to some 699,000 customers in a 1,700 square mile service territory which encompasses the greater Cleveland area as well as all or parts of nine northeastern Ohio counties. As a public utility and an electric light company within the definitions of Sections 4905.02 and 4905.03(A)(4) Revised Code, applicant is subject to the jurisdiction of this Commission pursuant to Sections 4905.04, 4905.05, and 4905.06 Revised Code. The company's present rates for electric service were established by the May 2, 1979 Opinion and Order of this Commission in Case No. 78-677-EL-AIR, as subsequently modified by the Order on Rehearing in that docket of March 5, 1980.

On June 19, 1979, the Cleveland Electric Illuminating Company served and filed a notice of its intent to submit a permanent rate increase application pursuant to Section 4909.18 Revised Code as required by Section 4909.43(B) Revised Code and Rule 4901-1-36 Ohio Administrative Code. As a part of this prefiling notification, applicant re-

quested that June 30, 1979, be fixed as the date certain for the valuation of property and that the twelve months ending December 31, 1979 be established as the test period for the analysis of accounts. The Commission approved the proposed date certain and test year by Entry of July 5, 1979. By motion of August 3, 1979, applicant requested a waiver of certain of the Commission's Standard Filing Requirements. This motion was granted in part and denied in part by Commission Entry of August 22, 1979. The application itself was filed September 17, 1979. The Commission accepted the application for filing by Entry of October 19, 1979, and approved the proposed form of the required legal notice subject to certain modifications.

On August 7, 1979, the Council of the City of Cleveland passed Ordinance No. 1673-79, which continued in effect the Illuminating Company's existing rates for service within that municipality for a two-year period commencing June 19, 1980. The company filed a complaint and appeal from said ordinance pursuant to the provisions of Section 4909.34 Revised Code on August 31, 1979. By Entry of September 26, 1979, the Commission determined that the evaluation of the complaint and appeal should be conducted with reference to the same date certain and test year previously approved in connection with the pending general rate application and that the two cases should be consolidated. The company submitted the information required by the Standard Filing Requirements on November 19, 1979, and the Commission, by Entry of December 12, 1979, accepted the complaint and appeal for filing as of that date. An amended proposed form of legal notice was approved for publication.

By its Entry of August 8, 1979, in Case No. 79-525-EL-ATA, the Commission approved the application of the Cleveland Electric Illuminating Company for authority to establish rates and terms and conditions of service for electric street lighting service. Proposed tariff sheets gov-

erning this service were accepted for filing pursuant to Section 4909.18 Revised Code as an application not for an increase in rates. However, in its Entry of October 5, 1979, issued in response to rehearing applications filed by certain affected municipalities, the Commission concluded that a rehearing should be granted for the purpose of reviewing the reasonableness of the new street lighting tariffs. The Commission directed that this matter be consolidated for hearing with the pending rate case.

In accordance with the provisions of Section 4909.19 Revised Code, the Staff of the Commission conducted an investigation of the matters set forth in the application and the complaint and appeal. A written report of the results of the staff investigation was filed March 4, 1980, and was served as provided by law. Objections to the Staff Report were timely filed by the applicant and by the following intervenors: the Office of Consumers' Counsel; the City of Cleveland, Senior Citizens, *et. al.*; Industrial Electricity Consumers; and the City of University Heights.

Pursuant to the Commission's Entry of March 12, 1980, the public hearing of these matters commenced April 2, 1980, before attorney examiner Barth E. Royer. The first day of hearing was held at City Hall in Cleveland, Ohio, to afford members of the public affected by these cases the opportunity to present statements concerning the proposed increase. Subsequent sessions were held at the offices of the Commission, 180 East Broad Street, Columbus, Ohio. The recorded transcript of the proceeding and the exhibits admitted into evidence during the 32 days of hearing have now been certified to the Commission by the examiner for its consideration.

**Appearances:**

Mr. Alan D. Wright, General Counsel, and Mr. Craig I. Smith, Senior Counsel, 55 Public Square, Cleveland, Ohio; and Messrs. Squire, Sanders & Dempsey, by Messrs.

Alan P. Buchmann, Lowell L. Garret, William C. Donahue, and Richard W. McLaren, Jr., 1800 Union Commerce Building, Cleveland, Ohio, on behalf of the applicant, the Cleveland Electric Illuminating Company.

Mr. William J. Brown, Attorney General of Ohio, by Messrs. Thomas L. Mumaw, David Neubauer, and James Bacha and Ms. Judith B. Sanders, Assistant Attorneys General, 180 East Broad Street, Columbus, Ohio, on behalf of the Staff of the Public Utilities Commission of Ohio.

Mr. James E. Wagner, Director of Law, and Mr. James L. Harkins, Jr., Assistant Director of Law, Cleveland City Hall, 601 Lakeside Avenue, Cleveland, Ohio; and Mr. Henry W. Eckhart, 88 East Broad Street, Columbus, Ohio; on behalf of the City of Cleveland, Ohio.

Mr. William A. Spratley, Consumers' Counsel, by Mr. Gary M. Petroff and Ms. Gretchen J. Hummel, Associate Consumers' Counsel, 137 East State Street, Columbus, Ohio, on behalf of the Office of Consumers' Counsel.

Mr. Joseph P. Meissner, Cleveland Legal Aid Society, 1223 West 6th Street, Cleveland, Ohio, on behalf of the Senior Citizens Coalition, the Cleveland Welfare Rights Organization, Inc., the Western Reserve Alliance, the Cleveland Chapter of Ohioans for Utility Reform, and North Shore Alert, intervenors.

Messrs. Bell & Clevenger, L.P.A., by Messrs. Langdon D. Bell, and Samuel C. Randazzo, 21 East State Street, Columbus, Ohio, on behalf of Industrial Electricity Consumers (Aluminum Corporation of America, Chase Brass and Copper Company, Inc., General Motors Corporation, Jones and Laughlin Steel Corporation, Olin Corporation, and Union Carbide Corporation), intervenors.

Mr. Guerin L. Avery, Law Director, Brainard Place-Suite 333, 29001 Cedar Road, Lyndhurst, Ohio, on behalf of the City of University Heights, Ohio, intervenor.

**Commission Review and Discussion:**

These cases come before the Commission upon the application of the Cleveland Electric Illuminating Company pursuant to Section 4909.18 Revised Code for authority to increase its rates and charges for electric service to its jurisdictional customers and upon the company's complaint and appeal pursuant to Section 4909.34 Revised Code from Ordinance No. 1673-79 of the City of Cleveland, Ohio, whereby it is charged that said ordinance, which would continue applicant's present rates in effect, is unreasonable and unlawful. Applicant alleges that its existing rates are insufficient to provide it reasonable compensation for the service it renders customers affected by these proceedings and seeks Commission approval of rate schedules which would yield some $79,795,000 in additional gross annual revenues based on its analysis of test-year operations. This additional revenue represents an increase of approximately 10.3 percent over that currently realized from service to jurisdictional customers. It now falls to the Commission to evaluate the evidence of record in order to determine if applicant's existing jurisdictional rates are inadequate and if the ordinance appealed from is unreasonable. In the event applicant is found to have sustained its burden of proof with respect to these matters, the Commission must then establish rates which will afford the company the opportunity to earn a fair rate of return.

Also before the Commission for consideration at this time is Case No. 79-525-EL-ATA, an application by Cleveland Electric Illuminating Company to establish rates and terms and conditions of service for providing electric street lighting within its service territory. Although the Commission has previously accepted this tariff as an application not for an increase in rates by its entry in this docket of August 8, 1979, specific provision was made in

its rehearing entry of October 5, 1979, for a review of the reasonableness of the rates contained therein in the context of the pending rate proceedings. We will address the street lighting matter through a separate opinion.

## JURISDICTIONAL ALLOCATIONS

In assigning rate base and demand-related expenses to the customers affected by the instant application and complaint and appeal, the applicant generally followed the two-peak allocation methodology accepted by the Commission in its prior case (App. Ex. 6B, p. 8). However, in developing the allocation factors to be used for purposes of these proceedings, the company used a projected summer and winter peak rather than relying on historical data for determining weighted seasonal peak demands. Further, applicant also adjusted the power plant capacity ratios to reflect an anticipated decline in nonjurisdictional load levels resulting from a reduction in contract demand associated with service to the Cleveland Department of Public Utilities (App. Ex. 6B, pp. 2-3). The staff recommends that these allocation procedures be rejected and proposes, in lieu thereof, a 12-month coincident peak method for determining demand allocation (S. R., pp. 3-6). Applicant has objected to the staff recommendation.

As the Commission has observed on prior occasions, there are a number of valid allocation techniques available; but the choice in a given case must turn on which of the methods proposed most accurately recognizes power cost causation in light of the operating characteristics of the utility in question (*Ohio Power Company*, Case No. 75-161-EL-SLF [August 4, 1976]). It should be apparent that the two-peak method is only appropriate for those companies which exhibit a pronounced summer and winter peak. Although applicant may have fit this description

in the past, the test-year data, as the staff points out, shows a leveling of the monthly peaks (S.R., pp. 4-5, Tr. XX, p. 117). The lowest actual 1979 monthly peak (October) was 87 percent of the highest monthly peak (July) (S.R., pp. 4-5). In six other months, the peak was in excess of 95 percent of the annual peak (App. Ex. 6C). When the 1979 monthly peaks are plotted graphically, it is evident that the peaks have become hills and that the valleys have filled in (Tr. XX, p. 117). If the Commission limits its analysis to this data, it is clear that the staff's 12-month coincident peak method should be preferred. Indeed, this is the method applicant uses before the Federal Energy Regulatory Commission, although, in fairness, it should be noted that the FERC apparently now requires the use of the 12-month method (S.R., p. 5, Tr. XV, p. 13).

Applicant attempts to justify its continued use of the two peak method by relying on estimates of the 1980 summer and winter peaks which, it contends, more accurately portray expected conditions. This novel approach is attended by several significant problems. First, from a conceptual standpoint, there should be some matching of the data sets involved in the determination of the allocation ratios and the property and expenses to which they are to be applied. After all, the purpose of the exercise is to assign existing plant based on existing demand, not to allocate future plant constructed to serve some future level of demand. However, quite apart from this theoretical consideration, is the question of the reliability of applicant's projections. The company attacks the staff method by claiming it does not adequately consider normal weather conditions (Tr. XX, pp. 113-115), an assumption automatically taken into account in applicant's forecast. No one disputes that temperature is a significant factor, but there are also other factors to be assessed such as the level of economic activity in the service territory, the

availability of the natural gas heating alternative, the impact of conservation efforts, the effect of rapidly increasing electric rates, and the track record of the company in predicting peak loads. On balance, the Commission does not believe that the test year data relied on by the staff is so unrepresentative as to yield an unreasonable result. Finally, we come to applicant's complaint that the staff method does not adequately consider daily operating characteristics because ten of the twelve monthly peaks were daytime peaks (App. Brief, pp. 27-28). Applicant attaches great significance to figures indicating that its daily load exceeds 90 percent of the daily peak for fifteen to nineteen hours on an average weekday basis (Tr. XV, p. 14). Because its projected winter peak is an evening peak, applicant contends that its method more properly weights the evening load's contribution to capacity requirements. This argument loses sight of the fact that both methods are peak responsibility methods and have nothing whatever to do with load duration. If applicant believes this diversity factor to be of such critical importance, the company should employ an allocation method specifically designed to recognize it rather than risk using a method which, in theory, could have resulted in the selection of two daytime peaks, thereby losing the evening load's contribution in its entirety. In fact, had applicant used calendar 1979 data, this would have been the case (App. Ex. 6C). The Commission does not believe that the staff method, which at least affords twelve measurements instead of only two, can be faulted on this score.

In light of the foregoing discussion, the Commission is of the opinion that the staff's 12-month method should be adopted for purposes of these proceedings. Although we do not view the fact that the FERC mandates the use of this method as being in any way controlling for the purposes at hand, there is a certain comfort in the sym-

metry resulting from using the same allocation method in both jurisdictions; the sum of the parts cannot be greater than the whole. Further, the Commission finds applicant's proposed adjustment to reflect the anticipated reduction in contract demand associated nonjurisdictional service to the Cleveland Department of Public Utilities to be inconsistent with the matching concept referred to above. Although the Commission would agree that this change will have some impact on the nonjurisdictional load, we cannot conclude that this will be the only factor affecting the jurisdictional-nonjurisdictional load mix during the period these rates will be in effect. Moreover, this minor change in the contract demand does not automatically mean that the actual demand will track the reduction precisely. The evidence indicates that during the test year, when the Cleveland Department of Public Utilities contract called for 80 megawatts, monthly peaks actually ranged from 69.4 to 90.0 megawatts (Staff Ex. 2, pp. 6-7). The possible effect of this single change is not enough to convince the Commission to shelve the test-year concept. We, therefore, accept as reasonable the allocation ratios proposed by the staff.

## RATE BASE

The applicant, the Commission staff, and Consumers' Counsel each offered testimony and submitted exhibits in support of their respective rate base proposals in these proceedings. The following table compares the company and staff estimates of the value of applicant's property used and useful in rendering the service affected by the application and the complaint and appeal as of the date certain of June 30, 1979. The adjustments to these proposals recommended by the various intervenors will be discussed on an item-by-item basis below.

**Jurisdictional Rate Base**

**(000's Omitted)**

| | Applicant[1] | Staff[2] |
|---|---|---|
| Plant In Service | $1,889,583 | $1,876,927 |
| Depreciation Reserve | (464,602) | (466,049) |
| Net Plant In Service | $1,424,981 | $1,410,878 |
| CWIP | 95,501 | 91,521 |
| Working Capital | 128,394 | 62,865 |
| Deferred Taxes and Tax Credits | (25,687) | (79,215) |
| Jurisdictional Rate Base | $1,623,189 | $1,486,049 |

[1]App. Rev. Sched. B-1

[2]Staff Ex. 7, Appendix D, Rev. Sched. 7.1

The difference between the respective plant in service determinations of the applicant and the staff is, in part, attributable to the difference in the allocation methodologies employed. There are, however, additional reasons for the discrepancy in these figures which must be explored, as well as other related issues arising from intervenors' objections which must be considered.

**Land and Land Rights:**

As a part of its investigation in these proceedings, the Commission staff reviewed the company's land accounts in order to assure that the real property proposed for inclusion in rate base satisfied the statutory used and useful requirement. Similar staff analyses in prior cases involving this company have resulted in some transfers to future use or non-utility property accounts, and the staff inspection of additional parcels in connection with the cases now before us has again produced a recommendation that the rate base be adjusted (S.R., pp. 21-22). Specifically, the staff concluded that a deduction in the amount of $368,938 was appropriate based on its finding that three ash disposal

sites associated with the East Lake plant were no longer used and useful and its opinion that the acreage at the Inland substation and Strongsville service center was in excess of that reasonably required for utility operations (S.R., p. 21; S.R., Sched. 8.2; Staff Ex. 2, pp. 8-11). Applicant objected to the deduction from rate base of the original cost dollars represented by these parcels and, through its witness Kemper, presented evidence in support of its position that the property in question was used and useful at date certain (App. Ex. 3A, pp. 4-7).

The staff excluded the Vine, Syracuse A, and Syracuse B ash disposal sites based on its conclusion that the capacity of these areas to receive fly ash had been exhausted. Applicant points out that one of the sites can still accommodate fly ash and is also being used to store cinders which are eventually sold to municipalities (App. Ex. 3A, p. 4). The Commission agrees that the value of this parcel, $25,499, must be restored to rate base. The Commission does not agree, however, that the other two ash disposal sites constitute used and useful property as contemplated by the statute. Applicant acknowledges that these two parcels are filled to capacity, but argues that they are still satisfying one of their original purposes, holding fly ash. Further, the company claims that the sites have little resale value and, because land is not depreciable property, there is no way that any cost recovery or return can be realized unless the parcels are included in rate base. There is no merit in either of these arguments. Property can only be considered used and useful if it is utilized in providing service. The record is clear that the two parcels in question can no longer receive fly ash; thus, they do not meet this requirement. Moreover, the fact that the parcels may have limited resale value is totally irrelevant. Once the property has been found not to be used and useful, it goes without saying that ratepayers cannot be required to contribute toward a return on it. The Commission, therefore, accepts

the staff's rate base adjustment for these two ash disposal sites.

The staff's proposed deductions for excess land at the Inland substation and the Strongsville service center present much closer questions (Staff Ex. 2, pp. 10-11). The Commission has previously recognized that there are a number of factors which must be considered in evaluating adjustments involving the elimination of minor portions of land parcels on the theory that the total acreage at a site is above that reasonably required to support a given installation (*Ohio Edison Company*, Case No. 78-1567-EL-AIR, *et al.* [January 30, 1980]). Obvious practical constraints exist upon obtaining precisely the acreage necessary for a particular operation, and there is a possibility that severance damages would actually produce a net detriment to the ratepayer if a somewhat smaller parcel had, in fact, been acquired. Although the site maps introduced by the applicant might appear to suggest the need for this type of analysis in this case (App. Ex. 3A, pp. 28-29), the Commission finds the critical evidence in this area to be the admissions of applicant's own witness with respect to the company's specified plans for the future use of much of the area excluded by the staff at these two locations (App. Ex. 3A, pp. 5-6). Given this state of the record, we conclude that the dollar associated with these areas should properly be assigned to Account 105 (Land Held for Future Use) until such time as the planned construction is accomplished. Applicant's objection to the staff adjustments should be overruled.

**Beaver Valley Common Facilities:**

In arriving at its recommended rate base for purposes of these proceedings, the Commission staff excluded from plant in service the amount of $8,894,241 which represents applicant's share of the common facilities at the Beaver Valley nuclear generating plant (S.R., p. 22; S.R.,

Sched. 8.1). Because applicant's ownership interest in Beaver Valley is limited to Unit No. 2, a unit still under construction, the staff concluded that it would be improper to consider the company's share of the common facilities, although completed in connection with the first Beaver Valley unit, as used and useful property until such time as Unit No. 2 is placed in service. Applicant objects to the staff's treatment.

The Commission has had occasion to consider this precise question in a number of its recent decisions, including that issued in this company's last rate case (*Cleveland Electric Illuminating Company*, Case No. 78-677-EL-AIR [May 2, 1979]; *Ohio Edison Company*, Case No. 77-1249-EL-AIR [November 17, 1978]; *Toledo Edison Company*, Case No. 79-143-EL-AIR [February 29, 1980]). We have repeatedly held the staff adjustment to be proper, and nothing presented in this record would persuade us to alter that view (App. Ex. 4, pp. 43-44). Although the Commission recognizes that FERC accounting principles require that common facilities be classified as plant in service at the time the first unit is placed in service, this does not change the fact that the common facilities in question do not satisfy the statutory criteria for rate base eligibility (Section 4905.15(A)(1) Revised Code). Cleveland Electric Illuminating Company does not own Beaver Valley Unit No. 1. Although applicant's customers may, from time to time, receive power from the first Beaver Valley unit by virtue of certain CAPCO transactions, this does not render the portion of the common facilities assignable to Unit No. 2 used and useful property for ratemaking purposes. This objection is again overruled.

Applicant contends that if the common facilities are to be eliminated from rate base, consistency requires that the Commission direct the company to reclassify this property as plant held for future use, to cease accruing depreciation, and to resume the accumulation of AFUDC until

such time as Unit No. 2 is transferred to plant in service (App. Ex. 4A, p. 49). The staff has also recommended a reclassification of the property (S.R., p. 22). In the *Toledo Edison* case, *supra*, the Commission agreed that the principles underlying the exclusion of the common facilities from rate base dictate that the property be reclassified for Ohio regulatory purposes and directed that depreciation accruals be stopped. The Commission did not reach the question of the resumption of AFUDC in the context of that decision, but believes that such a measure would be inconsistent with the classification of the property as plant held for future use. The Commission, therefore, orders applicant to reclassify the Beaver Valley common facilities and to cease accruing depreciation. Applicant's proposal to resume AFUDC must be rejected.

**Davis-Besse Nuclear Plant:**

Through their filed objections, intervenors City of Cleveland and Senior Citizens *et al.*, contend that applicant's share of the Davis-Besse nuclear plant, a generating facility co-owned by Cleveland Electric Illuminating Company and Toledo Edison Company, should be excluded from the rate base on the theory that the plant is not "used and useful" within the meaning of that term as employed in Section 4909.15(A)(1) Revised Code. The Commission is on familiar ground in considering these objections as the City of Cleveland advanced similar arguments in the company's last rate proceeding (*Cleveland Electric Illuminating Company*, Case No. 78-677-EL-AIR [May 2, 1979]). The Commission's finding in that case that Davis-Besse was properly includable in rate base has just been affirmed by the Supreme Court (*City of Cleveland v. Public Utilities Commission*, S.Ct. Case No. 79-1158 [July 9, 1980], 63 Ohio St. 2d [1980]). Although a considerable portion of the record now before us is devoted

to this question, when the law and the evidence are sifted out from the rhetoric and the statements of counsel, the Commission once again comes to the same inescapable conclusion. Davis-Besse must and should be included in the rate base. This is a most difficult issue to address, not because it presents a close question, but because much of intervenors' attack is so illogical as to defy analysis (See, Tr. XXIII, pp. 73-81).

Rather than begin with counsel for the City of Cleveland's repeated charge that Davis-Besse is a "white elephant" that is unsafe and unreliable (City of Cleveland Brief, p. 4), it may prove more fruitful to begin with an unimpassioned look at the facts. No one, including company witnesses who were examined on the subject, disputes the fact that the unit's 1979 performance was extremely disappointing (Tr. VIII, p. 67). The plant actually produced only some 59 percent of its budgeted generation during the test year (Senior Citizens Ex. 1). It exhibited a unit capacity factor in 1979 of only 39.4 percent (City of Cleveland Ex. 2L). Davis-Besse was forced off line 15 times during the test period, although in five of those instances the duration of the outage was less than one day (City of Cleveland Ex. 8). The principal reason for the unit's poor annual availability factor was the 103-day shutdown mandated by the Nuclear Regulatory Commission in the wake of the Three Mile Island incident (City of Cleveland Ex. 8). In terms of production expense, Davis-Besse is by far the cheapest source of energy available to the company (City of Cleveland Ex. 4). Despite the three month outage referred to above and another extended outage in December of 1979, the unit contributed over 1.6 billion Kwh to applicant's system generation during the test year, roughly 10 percent of the company's total production (City of Cleveland Ex. 4). Where, in these facts, is there support for the proposition that Davis-Besse is not used and useful?

Senior Citizens, *et al.*, suggests that if the plant cannot be excluded from rate base in its entirety, then, at minimum, the Commission should eliminate a portion of its value based on a calculation comparing its actual performance to its expected performance. The contention that utility property may be considered partially used and useful for rate base purposes is akin to the suggestion that someone can be partially pregnant. There is a well-established regulatory technique for dealing with the situation in which a generating unit exhibits an unusually high forced outage rate during the test year. The proper response is not the exclusion of all or part of the plant from rate base, but rather a normalizing adjustment to test period operations which excludes the costs associated with the outages in the calculation of future rates. This is precisely what the applicant and the staff have proposed in this case (App. Ex. 1, Sched. 3.12; S.R., p. 12). The approval of such an adjustment for ratemaking purposes places the ratepayers in exactly the same position with respect to future rates as if the plant had operated at anticipated levels.

At this point, intervenors' arguments became more difficult to comprehend. The Commission assumes they understand that operations have been normalized, so they must be suggesting that even if the plant performed as expected, it should still be excluded from rate base. Intervenors assert that the plant is unsafe and suffers from significant design and construction defects. The Commission is, of course, concerned about the risks associated with nuclear generation in general, and Davis-Besse in particular; but this is an area where the federal government has clearly pre-empted state regulatory authority. *Northern States Power Co. v. Minnesota*, 447 F.2d 1143 (8th Cir., 1971), *aff'd*, 405 U.S. 1035 (1972). *See also, Stebbins v. Public Utilities Commission*, S.Ct. Case No. 79-1622 (June 25, 1980), 62 Ohio St. 2d(1980). Moreover, nothing in this record indicates that the plant is unsafe.

What the evidence does show is that in each instance where a problem forced the unit off line, the problem was identified, reported, and remedied to the satisfaction of the Nuclear Regulatory Commission, the agency that does have authority in this area. It is true that the NRC has ordered a number of modifications, and that some of these have been quite costly (Tr. XXIII, p. 130); but it must be remembered that the plant has been subject to NRC scrutiny since the time it was on the drawing board and that it was and is licensed to operate.

Subsequent to the Commission order in the company's last case, the Supreme Court of Ohio issued its decision in *Consumers' Counsel v. Public Utilities Commission*, 58 Ohio St.2d 449 (1979). This case represented an appeal of a Toledo Edison rate order (*Toledo Edison Company*, Case No. 76-1176-EL-AIR [June 9, 1979]) wherein the Commission had determined that the Davis-Besse plant should be considered used and useful and, therefore, includable in rate base despite the fact that it had not been assigned commercial operating status before the date certain. The Commission based this conclusion on the fact that the unit had been synchronized with the system and was producing electricity, albeit through test generation, prior to date certain. The Court reversed, finding as follows:

> "It would be inequitable to prematurely shift the risk of plant failure from the utility's investors to the ratepayers by the inclusion in the rate base of highly complex and innovative technology which has not been proven to be reasonably free from significant design or construction defects. The initial risk of failure is appropriately borne by the investors, who have undertaken the project and who will ultimately profit from its success. It is only proper that their venture be found operational before they commence to recoup their capital outlays from the consumers." *Consumers' Counsel, supra*, pp. 456-457.

Intervenors, consistent with their assertion that the plant is unsafe, place great emphasis upon this language

as support for the proposition that Davis-Besse should not be included in the rate base in this case. However, the fact pattern presented to the Court in *Consumers' Counsel, supra*, was quite different than that with which the Commission is confronted in the instant proceedings. In that case, although there was test generation, the unit was not producing net energy for the consumer before the date certain. Here, the plant in question has been operational since 1977; the date certain was June 30, 1979. It has produced vast quantities of energy during that period of time. This is not a date certain timing problem of the type addressed by the Court. Further, if the Commission were to deny the company a return on Davis-Besse, consistency would require that test-period operations be adjusted to reflect an assumption that the plant was not available. We doubt that consumers would appreciate the impact of such a measure.

The City of Cleveland accuses the Commission of failing to recognize that applicant's share of Davis-Besse ended up costing about four times more than the company originally expected (Tr. VIII, p. 74) and that if these costs, plus the costs still being incurred to meet changing NRC requirements, are taken into account in computing costs per Kwh, Davis-Besse is no bargain. Intervenor goes so far as to assert that "the capital costs associated with Davis-Besse are the primary cause of the CEI financial problems" (City of Cleveland Brief, p. 4). Assuming for the sake of argument that this statement is correct, how would the exclusion of the plant from rate base do anything but exacerbate these problems? The fact is that the capital costs associated with the construction of all types of capacity have skyrocketed (Tr. VIII, p. 61). Although the problem is more acute with respect to nuclear plants due to ever-tightening licensing requirements, the hope was and is that the output from Davis-Besse over its life will cost substantially less than any alternative construction the company could have undertaken in the same time frame

(Tr. VIII, p. 69). The relevant point is that the investment in the plant has been made, the plant is providing service, and the suppliers of the required capital are entitled to a return on their investment.

There are other inconsistencies in intervenors' arguments that should not go unnoticed. The City of Cleveland complains that it costs the ratepayers approximately $800,000 per week for each week the plant does not operate (City of Cleveland Brief, p. 3). Which way does this cut? We would have thought that this testifies to the benefit of having Davis-Besse on the system. Then, there is the suggestion by Senior Citizens, *et al.*, that the uncertainties associated with Davis-Besse increase risk, thereby driving up investors' return requirements (Senior Citizens Brief, p. 21). We would merely inquire as to what impact on the company's cost of capital intervenor would anticipate were the Commission to disallow any return on the tremendous investment in this plant as it would have us do. Finally, we come to the theory that if the Commission includes Davis-Besse in rate base, the company will have no incentive to seek legal redress for any losses occasioned by the alleged defects in the design or construction of the unit or by the alleged negligence of Toledo Edison personnel in managing its operation. Senior Citizens'. *et al.*, even suggests that if the Commission recognizes Davis-Besse for ratemaking purposes, such a step would afford a defense in any legal action that applicant might maintain. These arguments are totally without merit. In the first place, they assume that the company has some actionable claim arising out of the unit's admittedly poor performance. It would certainly be improper for the Commission to engage in speculation in this area, and even more improper to base a rate case deduction on the innuendo of intervenors' attorneys. Detailed contracts and agreements govern applicant's relationship with those firms that constructed and operate Davis-Besse. Intervenors should examine their provisions before spread-

ing these assertions on the record. The Commission cannot deny applicant a return on this plant at this point in time with the instruction that it go sue someone or other in hopes that it will recover something from them in the future. If it should eventuate that applicant does obtain some recovery through litigation, whether involving Davis-Besse or any other aspect of its operation, under circumstances where customers are entitled to share in the benefits the Commission will see to it that they are properly credited (*Ohio Power Company*, Case No. 77-380-EL-FAC (February 7, 1979); *Ohio Power Company*, Case No. 78-676-EL-AIR [April 16, 1979]). There is simply no basis in law or fact for excluding all or part of the net original cost of Davis-Besse from the rate base determined for purposes of these proceedings.

**Excess Capacity:**

The Commission staff, as a part of its investigation in these proceedings, examined applicant's generating capacity to determine whether capacity exists which exceeds that reasonably required to meet the company's net peak demand and afford a reasonable reserve margin. As a result of this review, the staff concluded that applicant's production system was not excessive (S.R., pp. 22-23; Tr. XXI, pp. 114-120). Intervenors City of Cleveland and Senior Citizens, *et al.*, object to the staff's finding, contending that the staff analysis was inadequate and that the company does have excess capacity. Claiming, without a shred of evidence as to why the figure should be accepted, that a 20 percent reserve margin is appropriate, intervenors propose a rate base deduction, never quantified, to exclude capacity in excess of this amount on the theory that such property is not used and useful. The short answer here would be to simply point out that there is nothing in this record, save for intervenors' bare assertions, that would support these objections. However, the Commission will

once again set out the considerations which must be taken into account in dealing with this question.

This so-called "excess capacity" issue has been before the Commission time and time again in recent years in cases involving almost all major electric companies subject to our jurisdiction, including this applicant. (See *e.g., Dayton Power and Light Company*, Case No. 76-823-EL-AIR [July 22, 1977]; *Monongahela Power Company*, Case No. 76-824-EL-AIR [September 7, 1977]; *Dayton Power and Light Company*, Case No. 78-92-EL-AIR [March 9, 1979]; and *Cleveland Electric Illuminating Company*, Case No. 78-677-EL-AIR [May 2, 1979]). One fact that has clearly emerged from these cases, as it has from the record in the instant proceedings, is that it is most inappropriate to measure the reasonableness of existing capacity levels by a simple comparison to some assumed ideal reserve margin (Tr. VIII, pp. 106-109; Tr. XXI, pp. 116-117). Reserve requirements are company-specific, and what is reasonable for one electric utility may not be reasonable for another depending on factors such as unit sizes and generation mix. Next, assuming appropriate reserve criteria can be established, it must be recognized that in light of the extensive lead times involved in the construction of generating facilities and the variety of factors which can influence load growth, it is obviously unrealistic to assume that any utility would have the forecasting capability which would allow it to add capacity in the precise increments required to maintain the theoretically appropriate margin. This problem is intensified by the large size of the units being added today. Thus, the relevant inquiry is not whether the reserve at any point in time matches some optimum margin, but whether, given all those factors which can influence construction and load growth, the company can be fairly said to have acted imprudently in its capacity planning. As we will discuss in more detail *infra*, there has been no showing that this has been the case with respect to this applicant.

Finally, there is the conceptual problem which attends a capacity adjustment based on the theory that a portion of a company's production capacity is not used and useful. All applicant's generating stations, although they may have been downrated or off line from time to time, were in service meeting customer demand pursuant to principles of economic dispatch during the test period. Thus, each unit, standing alone, clearly would meet the used and useful requirement. A percentage adjustment to system capacity ignores the reality that such capacity is comprised of individual units which represent actual substantial dollar investments committed to assure that adequate service can be maintained. As the Commission stated in the *Columbus and Southern* decision cited above:

> "Hindsight is always perfect, and before the Commission will consider denying a return on property actually used in providing service something more need be shown than that the company's foresight was not."

Intervenors' objections are, hereby, overruled.

**Depreciation Reserve:**

Section 4909.05(H) Revised Code requires that the Commission determine the proper and adequate reserve for depreciation to be deducted from the original cost of applicant's used and useful property. The staff, in the course of its investigation, tested applicant's booked reserve against a theoretical reserve study based on date certain balances and found excellent correlation, indicating that the booked reserve might properly be relied on for ratemaking purposes (S.R., pp. 23-24). The staff did take exception, however, to a retroactive adjustment to the reserve performed by applicant in order to reflect the change to the units-of-production method of depreciation for the nuclear plant accounts as authorized by this Com-

mission in *Determination of Depreciation Charges*, Case No. 77-1389-EL-UNC (December 12, 1979). The Commission considered this same question in its order in *Toledo Edison Company*, Case No. 79-143-EL-AIR (February 29, 1980), finding such an adjustment to be appropriate. The staff revised its recommendation at hearing to conform to that decision and this step, together with a correction to reflect normalized generation for Davis-Besse, essentially removes the matter from controversy (Staff Ex. 2, pp. 11-12). The remaining differences between the applicant and staff reserve recommendations are tied to their respective positions on certain other rate base, allocation, and normalization issues. As those questions have been resolved in favor of the staff, the Commission adopts the staff's proposed jurisdictional depreciation reserve of $466,049,256 as the proper deduction from plant in service for purposes of these proceedings (Staff Ex. 3, Rev. Sched. 9). Deducting this amount from the original cost of includable property results in a finding of jurisdictional net plant in service of $1,410,903,292.

**Construction Work In Progress:**

Section 4909.15(A)(1) Revised Code provides that the Commission, in its discretion, may include in its rate base determination a reasonable allowance for construction work in progress. The statute limits eligibility for the allowance to projects which are 75 percent complete, and there is a further prohibition against authorization of such an allowance to the extent it would exceed 20 percent of the total valuation not including this item (Section 4909.15 (E) Revised Code). For purposes of these proceedings, applicant originally requested an allowance for construction work in progress of $99,263,076, which reflected the jurisdictional date certain costs associated with some 171 job orders considered by the company to represent qualifying projects (App. Ex. 1, Sched. B-4). The requested

allowance was subsequently reduced to $95,501,269 in light of applicant's acceptance of a staff adjustment which reclassified 48 of the job orders based on a finding that the construction in question was complete and the property in service at date certain (App. Ex. 3A, p. 28; App. Rev. Sched. B-1). The staff recommends a jurisdictional allowance of $91,521,464 (S.R., pp. 24-25; S.R., Sched. 10). Consumers' Counsel, although opposed in principle to an allowance for construction work in progress, has accepted the staff's recommendation as reasonable (O.C.C. Ex. 1, pp. 7-8); but the City of Cleveland and Senior Citizens, *et al.*, contend that there should be no construction work in progress allowance authorized in these cases.

The claims of the intervenors opposing any allowance for construction work in progress require no more than a cursory discussion, as much of what has been argued here has been heard and rejected many times in the past (See *Ohio Edison Company*, Case No. 78-1567-EL-AIR [January 30, 1980] and cases summarized therein). Senior Citizens' contention that the statute creating the allowance is unconstitutional has been definitively laid to rest (*Consumers' Counsel v. Public Utilities Commission*, 58 Ohio St. 2d 108 [1979]), and its charge that the Commission is "stumbling along" trying to define some standards for the exercise of the discretion conferred by Section 4909.15(A)(1) Revised Code is unfounded (*Ohio Edison Company, supra*). Intervenors' specific objection to the inclusion of Project No. 1974 IBM, applicant's share of Unit No. 3 at the Bruce Mansfield generating station, does warrant some comment. This item constitutes some $90 million of the total allowance requested and there is no dispute that the project meets all the statutory eligibility criteria (App. Ex. 1, Sched. B-4). However, in keeping with their assertion that the company already has excess generating capacity and their opinion that applicant has demonstrated no compelling financial need, the City of Cleveland and Senior Citizens, *et al.*, urge the Commission

to ignore this substantial capital investment in establishing rates in this case. Given our perception of the purpose of the statutory provision allowing consideration of construction work in progress as explained in *Columbus and Southern Ohio Electric Company*, Case No. 77-545-EL-AIR (March 31, 1979), and recently reiterated in *Ohio Edison, supra*, we would think that there would be less room for argument concerning the propriety of including Mansfield Unit No. 3 than any other of the items for which applicant has requested recognition. In light of the Commission's rejection of intervenors' excess capacity theory and consistent with our prior holdings with respect to proposed "overwhelming need" standards, the Commission overrules these objections (*Dayton Power and Light Company*, Case No. 76-823-EL-AIR [July 22, 1977]; *Cleveland Electric Illuminating Company*, Case No. 78-677-EL-AIR [May 2, 1979]).

As indicated above, the difference in the applicant and staff construction work in progress recommendations is relatively minor, and part of the remaining disparity is attributable to the difference in the allocation methods employed. Yet despite the comparatively small total dollar difference between the respective proposals, there are some 76 individual job orders still in dispute (S.R., p. 25). The basis for applicant's objection to the staff exclusion for each of these items is set out in the testimony of applicant's witness Kemper (App. Ex. 3A, pp. 10-28). Given the obvious constraints which preclude the Commission from proceeding with an individual analysis of each one of these job orders within the confines of this written opinion, we believe it reasonable to resolve the matter through a more general discussion. In light of the fact that the Commission has previously indicated that it believes the purpose of the allowance to be to recognize the existence of major new construction projects, it is tempting to simply eliminate a number of these items as not constituting the type of evidence contemplated by the

statute. However, the staff has inspected each of these items and has offered additional reasons why they should not be considered (Staff Ex. 1, pp. 3-18). Nothing in this record would persuade us that the allowance recommended by the staff is unreasonable.

Applicant begins its criticism of the staff's findings by suggesting that the Commission should, as a matter of policy, recognize in the allowance any expenditures relating to efforts to improve power plant productivity or required by various governmental agencies for environmental or safety reasons (App. Ex. 3A, p. 9). The unfortunate negative implication of this recommendation is that if the Commission fails to adopt these criteria it is unconcerned about applicant's productivity, the environment, or the public safety. We trust that all concerned will recognize this smoke screen for what it is and will realize that the real issue here is whether or not the expenditures represent qualifying construction projects under the statute and our past decisions.

Review of the testimony of staff witness Weiss indicates that the reasons underlying the staff's exclusion of the projects now in issue fall in four basic categories (Staff Ex. 1, pp. 3-18). Some were excluded because the staff found them to be less than 75 percent complete. Several were eliminated upon a finding that they represented a purchase rather than a construction project. Others were excluded because they were of a replacement nature. Finally, there were exclusions based on the conclusion that the expenditures involved were more properly associated with maintenance rather than construction. In several instances, the exclusion was tied to more than one of these reasons. Each one of the identified criteria has been recognized by the Commission in past cases as representing an appropriate standard by which to test the eligibility of specific expenditures for inclusion in the construction work in progress allowance (S.R., p. 25). Moreover, the Commission has also pointed out that there is

judgment involved in applying every one of these tests. Despite the complaints from those who would have the Commission establish rigid rules to be strictly applied in every case, we continue to believe that judgment must play an important role in determining what evidence is properly considered in authorizing an allowance for construction work in progress in a given case.

For purposes of illustration, consider the Commission's determination that items which constitute purchases are not construction projects within the meaning of the statute. The logical foundation of this standard is so clear that an explanation is almost superfluous. An item acquired by a utility through a single-payment transaction is either in service at date certain and, therefore, in rate base, or it is not, and no return may be earned on it. A purchase is not construction, nor is it a project. Applicant's job order no. 50030, a caterpillar tractor-scraper acquired for use at one of the company's power plants, is a clear-cut example of a purchase (App. Ex. 3A, p. 23). It was properly excluded by the staff (Staff Ex. 1, p. 14). But compare this situation to job order no. 50228, a crawler tractor purchased and delivered prior to date certain but which required additional company labor before it was ready for use (App. Ex. 3A, p. 22; App. Ex. 3B). Does this change its essential nature from a purchase to a construction project? The Commission would agree with the staff conclusion that it clearly did not (Staff Ex. 1, p. 13), but there is now an element of judgment involved.

This same element of judgment is also present to some degree in each of the other tests the staff employed. The staff's finding that several of the job orders proposed for inclusion by applicant were not 75 percent complete followed from the staff's opinion that these items, because of their scope and purpose, should be examined individually and not considered as a part of a larger project as the company had suggested (Staff Ex. 1, p. 7). The exclusion

of items on the ground that they represent replacement projects or maintenance work also requires that a view be taken as to the basic characteristic of the expenditure (See *Toledo Edison Company*, Case No. 79-143-EL-AIR [February 29, 1980]). In each instance, the Commission believes the treatment recommended by the staff to be consistent with the intent of the statute and, therefore, finds that the construction work in progress allowance proposed by the staff should be adopted for purposes of these proceedings. Those items excluded are not properly defined as major new construction when the amount of the obligated capital involved is considered in connection with time period for which it has been committed and the purpose to which it has been put. Applicant's objection is overruled.

**Working Capital:**

The applicant, the staff, and Consumers' Counsel each proposed an allowance for working capital to be included in the rate base valuation in accordance with the provisions of Section 4909.15(A)(1) Revised Code. All three estimates were derived through the use of the formula approach, but there are significant differences between the results of the respective calculations. Applicant requests an allowance of $128,393,775 (App. Rev. Sched. B-1), while the staff's recommended allowance is $62,865,000 (Staff Ex. 7, Rev. Sched. 7). Consumers' Counsel's calculation resulted in a proposed allowance of $56,935,000 (O.C.C. Ex. 1, Rev. Sched. JTC-2). Issues exist with respect to each element of the formula which we will address, in turn, below.

The difference in the cash component of the formula as presented by the parties is, in part, the product of the sponsors' respective positions on various expense issues and, in some measure, created by the difference in allocation methods. The most significant difference, however,

arises from the fact that the applicant failed to exclude fuel expense from operation and maintenance expenses in computing its proposed cash allowance. Staff witness Hanna and Consumers' Counsel witness Chapski both believe this deduction to be appropriate (Staff Ex. 7, p. 12; O.C.C. Ex. 1, pp. 12-13). Much of the debate on this point has centered on applicant's complaint that fuel expense was not deducted under the original formula as propounded by the FPC (now FERC) (App. Brief, p. 12). Be that as it may, it is clear that this Commission has consistently excluded fuel expense under its version of the formula for some years, and, in most instances, without objection from the utility involved (See, *e.g.*, *Ohio Edison Company*, Case No. 78-1567-EL-AIR [January 30, 1980]). The Commission has cited as one of the virtues of the formula method for determining a working capital allowance that it assures evenhanded treatment among rate applicants (*United Telephone Company of Ohio*, Case No. 72-995-Y [September 9, 1974]). It has never suggested that the formula does more than approximate the result of a full-blown lead-lag study. If applicant wishes to depart from this formula on the grounds that it does not properly recognize one item or another, we suggest that it support this claim with a properly conceived lead-lag study which examines all the timing differences involved between when expenses are incurred and payments are received. Applicant's objection is overruled.

The applicant and the staff utilized the date certain balance for purposes of determining the materials and supplies component of the working capital formula. Consumers' Counsel witness Chapski used the average of thirteen monthly balances in arriving at his recommendation with respect to this component, a technique approved by the Commission on numerous past occasions, including this company's last rate case, on the grounds that it may

produce a more representative allowance. The staff has indicated that one of the reasons it utilized the date certain balance in this case was that actual test-year data was not available at the time of its audit (Tr. XXI, pp. 174-175). This data is now available to the Commission through Senior Citizen's Ex. 10, and the Commission concludes that the thirteen monthly balance method may properly be adopted utilizing the information contained therein. Jurisdictional materials and supplies calculated on this basis total $19,034,217. This amount must then be adjusted to eliminate those materials and supplies held for new construction, extensions and additions in accordance with the decision of the Supreme Court in *City of Cincinnati v. Public Utilities Commission*, 160 Ohio St. 2d 393 (1954), and the consistent practice of the Commission in implementing that decision. Applicant objects to this adjustment, claiming that the materials and supplies inventory is not maintained with a view as to the ultimate purpose to which individual items may be put (Tr. II, p. 83). This may well be true, but it certainly does not preclude an after-the-fact analysis of the use to which the items are actually put (S.R., Sched. 11A). The Commission finds the staff adjustment to account for this consideration to be reasonable and proper in all respects. Application of this adjustment factor to the inventory as determined above produces an allowance for materials and supplies of $16,491,246 which we deem reasonable for purposes of determining the working capital allowance to be authorized in these proceedings.

The fuel inventory allowance is composed of three separate items: oil, coal, and deferred nuclear fuel. Differences exist in each of these areas. Applicant based its proposed allowance for oil on a targeted capacity supply level of 90 percent (App. Ex. 5A, p. 13). The staff and Consumers' Counsel are in general agreement that 78 percent of capacity represents a more reasonable inventory

level in light of the company's actual experience (S.R., p. 25; Staff Ex. 6, p. 7; O.C.C. Ex. 1, p. 11). Applicant's witness Chopp was unable to explain the derivation of the the 90 percent target, nor was he aware if 90 percent of tank capacity had ever actually been achieved (Tr. II, pp. 98-100). It was certainly not achieved in the test year. Under these circumstances, the Commission believes the staff's proposed allowance for the oil inventory is on much firmer footing, and we will accept the staff's recommendation with respect to this component of the fuel inventory allowance.

The determination of the proper allowance for the coal inventory has been a subject attended by considerable debate in these proceedings. Applicant originally based its proposed allowance on the assumption that a 63.33-day supply represented a reasonable inventory balance (App. Ex. 5, pp. 16-17). This number was derived through what can only be described as a rather primitive analysis based on the assumptions that the company maintains a 50-day supply in a normal year and a 90-day supply during a year in which a UMW contract is up for renewal. As the miner's contract runs for a three-year period, the calculation assumed two years at the 50-day level and one year at the 90-day level producing a weighted average of 63.33 days. Cross-examination by counsel for Senior Citizens, *et al.*, quickly pointed up the flaw in this logic, as it is apparent that even if one accepts the validity of the general approach, a 90-day supply would not be maintained throughout the third year, but would gradually be built up in anticipation of a possible strike and would dissipate as the threat of the strike passed or as the reserves were called on in the event a work stoppage actually occurred. Mr. Chopp conceded the point (Tr. III, pp. 55-57). This prompted applicant to revise its calculation, this time assuming a 50-day supply in the first two years and a gradual build up and decline in the third year. The resulting weighted average became 55.3 days (App. Ex. 5G), and, based on this

calculation, the company now claims a 55-day coal inventory to be a reasonable basis for establishing the coal allowance. Rather than engage in this speculation, both staff witness Hefner and Consumers' Counsel witness Chapski pegged their recommended allowances to the actual experience of the company. Mr. Hefner, based on date certain data, a review of the monthly balances, and consideration of applicant's budget as it related to coal procurement concluded that a 45-day supply was reasonable (S.R., p. 25; Staff Ex. 6, pp. 6-7; Tr. XXI, pp. 48-49). Mr. Chapski simply relied on the average of the thirteen monthly balances, December, 1978, through December, 1979, in arriving at his recommended allowance which is slightly below that proposed by the staff in terms of actual dollars (O.C.C. Ex. 1, p. 11).

Applicant challenges the conclusions of these witnesses on several counts. The company argues that the use of test-year data is inappropriate, asserting that coal inventory levels in 1979 were lower than normal due to uncertainties arising from questions as to what low sulphur-high sulphur coal mix would be permitted (App. Ex. 5A, p. 14) and due to the fact that the current UMW contract was only in its second year. Applicant presented an exhibit showing that the monthly balances from the three-year period 1976 through 1978 averaged 53 days (App. Ex. 5B). However, when the 1979 data is added to this table a somewhat different picture emerges (Tr. VI, pp. 69-70). Although applicant claims that test-year inventory levels were lower than normal, the 1979 average of the monthly balances, 37.4 days, is actually higher than the 1978 average of 36.5 days (App. Ex. 5B). These numbers are both quite different from the 50-day supply applicant contends should be associated with the years where no strike is imminent. Certainly a plausible interpretation of this data is that the company considered the inventory remaining at the conclusion of the strike in March of 1978 to be reasonably adequate under the circumstances. If one employs appli-

cant's three-year weighted average approach using actual data rather than the assumed inventory levels utilized by the company, the results confirm the reasonableness of the staff's recommended allowance. The average monthly balance for 1977, the year of the strike, constituted a 66.3-day supply. Adding this to twice the 1978 average of 36.5 days and dividing by three yields a 46.4 day supply, a far better match with the staff's 45-day supply than with the company's 55-day recommendation.

Applicant's witness Chopp described the 45-day supply recommended by the staff as being "dangerously close" to the 40-day level specified by the Commission in Case No. 77-1139-EL-COI as the point at which the Company is permitted to abandon economic dispatch (App. Ex. 5A, p. 14). Taken at face value, this might be cause for concern; but the fact is that the company never had a 40-day monthly balance from March of 1978 through July of 1979 (App. Ex. 5B). As the staff points out on brief, the 40-day trigger becomes important only during the period of a strike where all utilities face the threat of service interruption (Staff Brief, p. 6). The Commission concedes that the 45-day supply recommended by the staff appears conservative in light of our findings in other recent electric cases, but we believe the staff recommendation to be the best supported on this record and will adopt the staff's proposed allowance for the coal inventory.

The remaining fuel-related issue to be considered is the appropriate allowance for deferred nuclear fuel. There are two separate questions in this area which must be resolved. Under the leasing agreement between the owners of Davis-Besse and the lessor of the nuclear fuel for the plant, applicant was required to begin payments for nuclear fuel in November 1976, whether or not the plant was in operation (App. Ex. 5A, p. 11). This plant actually was not placed in service until almost a year later, and additional time elapsed before final approval from the Nuclear Regulatory Commission to operate it at full load

(App. Ex. 5A, p. 12). The jurisdictional value of the investment in the fuel core is, of course, properly included in the working capital allowance. This balance is subject to reduction as payments are made to the lessor. Proper accounting dictates, however, that the nuclear fuel be expensed at the time when the fuel is consumed, even though the lease payments are actually made monthly under the terms of the contract (App. Ex. 5, p. 10). Thus, those payments made prior to the commercial operation of the plant are being amortized over the actual fuel burn-up (App. Ex. 5, p. 15). Applicant charged AFUDC on the payments made during this period (App. Ex. 5A, p. 12). The staff recommends that this AFUDC component, $228,835, be eliminated for purposes of determining the working capital allowance, contending that AFUDC was not properly chargeable on these payments as they do not represent construction costs of the type subject to AFUDC accumulation (Staff Ex. 7, p. 21; Staff Ex. 3, Rev. Sched. 11). The Commission agrees that this component should be eliminated. In so finding, we do not in any way suggest that applicant acted imprudently in entering into the leasing arrangement at the time it did, but we do not believe it consistent with the concept of a reasonable working capital allowance to charge ratepayers with these additional costs. Applicant's objection is overruled.

The applicant and the staff relied on the date certain balance for purposes of determining the allowance for deferred nuclear fuel (App. Ex. 1, Sched. B-5.1; Staff Ex. 3, Rev. Sched. 11). Consumers' Counsel used the average of thirteen monthly balances, which produced a somewhat lower figure (O.C.C. Ex. 1, p. 11). Senior Citizen's *et al.*, objects to these methods, arguing that they improperly charge ratepayers for increases in the balances caused by the extended outage of Davis-Besse in the late spring and early summer of last year (Senior Citizens Brief, pp. 9-10). As explained above, because nuclear fuel is expensed only when it is actually consumed, the balance will increase

under the operation of the lease in those periods when Davis-Besse is not on line. As intervenor correctly observes, the date certain balance is the second highest of the test-year monthly balances (App. Ex. 5E). As other aspects of test-year operations have been normalized so as to protect ratepayers from charges attributable to the unit's poor performance, we see no reason why the allowance for deferred nuclear fuel should not be accorded similar treatment. Applicant's witness Chopp agreed that there was no theoretical difference between such an adjustment and those made in other areas (Tr. VI, pp. 67-68). The evidence now before us will not permit the Commission to precisely calculate such an adjustment, but we believe a reasonable proxy for a normalizing adjustment of this type to be to establish the allowance for deferred nuclear fuel with reference to the average of the thirteen monthly balances adjusted so as to eliminate the three months of the TMI-related shut down (App. Ex. 5E). The results of this calculation produce a jurisdictional average of the ten remaining monthly balances of $7,013,586. The Commission is of the opinion that this represents a reasonable allowance for deferred nuclear fuel.

The largest single cause of the disparity between the applicant's working capital recommendation and that proposed by the staff and Consumers' Counsel stems from the fact that applicant failed to include an offset to the working capital allowance to reflect the availability of accrued taxes as required by the decision of the Supreme Court in *Cleveland Electric Illuminating Company v. Public Utilities Commission*, 42 Ohio St. 2d 403 (1975). Applicant has presented nothing new in support of its objection to the offset; in fact, it has presented almost nothing at all. Consumers' Counsel's objection that the offset should include FICA taxes has also been disposed of by prior Commission decisions (See *Columbus and Southern Ohio Electric Company*, Case No. 77-545-EL-AIR [March 31, 1978]). The tax offset proposed by the staff is hereby approved.

The final area of disagreement relates to the deduction for customer deposits required by the decision of the Supreme Court in *Consumers' Counsel v. Public Utilities Commission*, 58 Ohio St. 2d 108 (1979). Applicant, consistent with its apparent theory that precedent should be ignored if it works to the company's disadvantage, made no such deduction. The staff, in accordance with prior Commission decisions, treated the jurisdictional customer deposit balance as an offset to working capital, while Consumers' Counsel contends that it should be subtracted directly from rate base. As the Court indicated in the *Consumers' Counsel* decision, *supra*, the practical effect of either technique is the same. The Commission finds the deduction of $833,000 proposed by the staff to be appropriate, and will express the deduction as a working capital offset for purposes of these proceedings.

The following schedule presents in summary form the Commission's determination of the allowance for working capital to be included in rate base for purposes of these proceedings. These figures take into account revisions necessary to reflect the disposition of those other issues which affect the allowance.

**Jurisdictional Working Capital Allowance**
**(000's Omitted)**

| | |
|---|---|
| Cash Element (⅛ of Adjusted Operation and Maintenance Expense, excluding Fuel and Purchased Power) | $ 20,335 |
| Materials and Supplies | 16,491 |
| Fuel Inventory (Including Deferred Nuclear Fuel) | 47,012 |
| Tax Offset (¼ of Adjusted Taxes, excluding FICA and deferred FIT) | (20,480) |
| Customer Deposits | (833) |
| Jurisdictional Working Capital Allowance | $ 62,525 |

**Accumulated Deferred Taxes and Tax Credits:**

In every rate order issued since interperiod tax allocation became permissible under Section 4909.15(A)(4) Revised Code, this Commission has reduced the rate base of normalizing utilities by an amount equal to the balance of accumulated deferred taxes and tax credits which may be deducted without loss of benefit under the applicable provisions of the Internal Revenue Code. Although this practice is consistent with the customary regulatory treatment of these items throughout the country (Tr. XI p. 3), the Commission continues to be subjected to theories advanced by applicant utilities as to why such an adjustment is improper or inappropriate. Mercifully, the barrage has slowed somewhat of late, and in this case applicant has primarily directed its objection to the amount of the deduction rather than to its propriety.*

The staff proposes a reduction to rate base in an amount equal to the date certain balance of jurisdictional accumulated deferred income taxes associated with liberalized depreciation (Account 282) and accelerated amortization (Account 281), and the date certain accumulated deferred investment tax credits (Account 255, 3 and 4 percent components only). (S.R., p. 26). The total deduction is $79,215,257 (S.R., Sched. 12). Applicant also reduced rate base to reflect these balances, but restricted its origi-

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* Applicant did again raise the now familiar "Congressional intent" argument considered and rejected by the Commission in the company's last rate case (Case No. 78-677-EL-AIR [May 2, 1979]). The Commission has no quarrel with applicant's interpretation that the tax credits involved were authorized to provide an incentive for capital investment; but the rate base deduction is not inconsistent with that intent (Staff Ex. 7, pp. 27-28). Congress has specifically indicated those circumstances under which a rate base deduction is not permitted without loss of the benefit, and the Commission has made no adjustment in those instances (Section 46(f), Internal Revenue Code).

nal adjustment to some 44 percent of that proposed by the staff based on a purported identification of the risk-related portion of the deferred amounts (App. Ex. 1, Sched. B-8; App. Ex. 4, pp. 45-48). Through his supplemental testimony, applicant's witness Maugans now proposes an even more limited reduction based on the theory that only the deferred amounts actually recovered through rates may properly be deducted from rate base (App. Ex. 4A, Appendix 6; App. Ex. 4A, pp. 33-38). The Commission finds neither of these arguments persuasive.

Able cross-examination by staff counsel made short work of the novel concept that a risk differential exists with respect to a portion of the deferred balances and credits which dictates that they be included in rate base (Tr. XI, pp. 2-33). Mr. Maugans apparently concedes that the accumulated deferrals represent interest-free capital and, as such, may properly be deducted from rate base (Tr. XI, p. 20). However, the witness then draws a distinction between the terms "interest-free" and "risk-free" in arguing that a return should be allowed on a portion of the balances (Tr. XI, p. 20). The risk to which Mr. Maugans makes reference in the risk that the ultimate tax liability associated with the deferrals will not be paid. This risk is so obviously a risk to the federal government as opposed to one borne by the investors that this matter merits no further discussion. Indeed, applicant has abandoned the argument on brief.

The alternative deduction presented through Mr. Maugan's supplemental testimony is based in language appearing in the Commission's decision in *Ohio Power Company*, Case No. 78-676-EL-AIR (April 16, 1979) to the effect that a determination must be made as to whether existing rates reflect normalization before a rate base reduction for deferred taxes can properly be made (App. Ex. 4A, p. 35). In light of this statement, Mr. Maugans attempted to calculate the portion of the deferred balances

which had actually been recovered through past rates and concluded that a rate base deduction of no more than $25,687,045 was appropriate (App. Ex. 4A, p. 37). Although there are very real problems presented by the assumption that the amount of the recovery through past rates can actually be identified, the Commission need not consider this point in view of our conclusion that applicant's reliance on the language cited is misplaced. First, the Commission would point out that the discussion in *Ohio Power, supra,* related solely to the question of the appropriate treatment of deferred taxes associated with Ohio Electric Company, a subsidiary of Ohio Power whose rates had not theretofore been subject to Commission review. Secondly, whether or not one believes the issue in that case to have been correctly decided, it is quite clear from other orders addressing this subject that the Commission has viewed the controlling factor to be that these deferred amounts are not investor-supplied sources of funds, without real concern as to whether they are theoretically provided by customers or by the federal government. In fact, in the very first rate decision following statutory authorization of normalization, the Commission approved a rate base deduction (*Dayton Power and Light Company,* Case No. 76-88-GA-AIR [July 22, 1977]). Certainly there had been no actual customer "funding" of the deferrals at that time. In essence, the deferrals operate as a continuing offset to the original cost of the property with which they are associated and should be so considered for rate-making purposes. The Commission is of the opinion that Section 4909.05(I) Revised Code contemplates this type of rate base adjustment, but even if in the absence of express statutory authority we would view the staff's deduction as an appropriate and necessary adjunct to our approval of interperiod tax allocation. Applicant's objection should be overruled.

**Rate Base Summary:**

In light of the foregoing discussion, the Commission finds the jurisdictional rate base as of the date certain of June 30, 1979, to be as set forth on the following table. This table also presents the Commission findings as to rate base properly attributed to the application area and the City of Cleveland under the staff's allocation methodology which we have heretobefore approved.

**Rate Base Summary**
**(000's Omitted)**

| | Total Jurisdiction | Application Area | City of Cleveland |
|---|---|---|---|
| Plant In Service | $1,876,953 | $1,302,137 | $ 574,816 |
| Depreciation Reserve | (466,049) | (323,352) | (142,697) |
| Net Plant In Service | $1,410,903 | $ 978,784 | $ 432,119 |
| CWIP | 91,521 | 62,976 | 28,545 |
| Working Capital | 62,525 | 43,619 | 18,906 |
| Deferred Taxes and Tax Credits | (79,216) | (54,514) | (24,702) |
| Rate Base | $1,485,734 | $1,030,866 | $ 454,868 |

## OPERATING INCOME

Applicant and the Commission's staff each submitted an analysis of test-year accounts reflecting the results of operations under the company's present permanent rates. Consumers' Counsel also submitted evidence in support of proposed adjustments to the staff's findings and several intervenors have challenged certain of the results of the staff audit through their filed objections. A number of the issues presented are identical to those heard and decided in the company's last rate case (*Cleveland Electric Illuminating Company*, Case No. 78-677-EL-AIR [May 2, 1979]),

as are the arguments advanced in support of the competing positions. The Commission sees no purpose to be served by another detailed analysis of these same questions and, where appropriate, will merely indicate that our determination is in accord with our prior decision.

**Operating Revenue:**

The staff found applicant would have realized gross annual operating revenues of $773,389,000 had its present permanent rates been in place throughout the test year (Staff Ex. 3, Rev. Sched. 1). Although applicant originally raised a number of issues with respect to the staff's revenue determination through its filed objections, revisions offered by the staff at hearing have served to remove most of these matters from controversy (Staff Ex. 3; Staff Ex. 4; Staff Ex. 7). The applicant and the staff now agree with respect to the annualization of fuel costs and revenues and this question requires no further review. Applicant will be directed to file base (or non-fuel) rates sufficient to compensate the company for the approved allowable expenses, exclusive of fuel costs includable under Rule 26, and yield the authorized return on rate base, based on test-year operations as analyzed herein (*Dayton Power and Light Company*, Case No. 78-92-EL-AIR [March 9, 1979]).

An issue does remain, however, with respect to applicant's proposal to amortize the revenue and expense impact of a change in the demand charges contained in the contract governing purchases from Ohio Power Company (App. Ex. 1, Sched. C-3.21; App. Ex. 7A, pp. 2-3). The staff recommends against such an adjustment, pointing out that the change, which became effective January 1, 1980, is out-of-period, and that the annualization of purchased power costs, even to year-end levels, has not been considered appropriate by the Commission (Staff Ex. 7, pp. 36-37). The staff also explains that the specific change

in the Ohio Power contract relates to short term and limited term purchases, many of which will be recovered through the fuel adjustment clause (Staff Ex. 7, p. 37). As the Commission found in our recent decision in *Toledo Edison Company*, Case No. 79-143-EL-AIR (February 29, 1980), the month-to-month and year-to-year fluctuations in purchased power expense may occur for a variety of reasons and there is no assurance that an annualizing adjustment of the type proposed by applicant will render purchased power expense any more reflective of future conditions than reliance on the test-year figures. Further, allowable purchased power costs under the fuel adjustment clause cannot be predicted because of the multitude of complex factors which govern recovery through that mechanism. Applicant's proposed adjustment does not adequately consider this point (Staff Reply Brief, p. 8). The Commission will accept the staff's recommendation in this regard.

**Labor Expense:**

There are several issues in these proceedings which fall under the general heading of labor expense. Specifically, they involve the annualization of union wage increases, the annualization of non-union wage increases, and the annualization of overtime expense. The staff annualized union and non-union wage increases in place at the conclusion of the test year, but did not annualize the effect of any increases in the overtime rate (S.R., Sched. 3.4). Applicant annualized union wage increases through the May 1, 1980 contract, and non-union and overtime through the completion of the test year (App. Ex. 1, Sched. C-3.4). Consumers' Counsel objects to the annualization of any non-union wage increases.

The Commission has addressed each of the issues presented in a number of its recent decisions. For purposes

of these proceedings, we accept the staff adjustment for union and non-union increases in accordance with our decisions in this company's prior case and in *Toledo Edison Company*, Case No. 79-143-EL-AIR (February 29, 1980). We reject applicant's annualization of the May 1, 1980 increase as it does not comply with the standards for such a post-test period adjustment as set out in *Columbia Gas of Ohio*, Case No. 77-1309-GA-AIR (May 24, 1979) and *Cincinnati Gas and Electric Company*, Case No. 79-11-EL-AIR (January 7, 1980). Although the per unit rate of the increase may be known with certainty, there is no assurance that changes in number of employees, budgeted hours, and employee mix will not lead to an overstatement of the costs properly matched with that level of service and productivity experienced during the test year (See *Columbia Gas of Ohio*, Case No. 76-704-GA-CMR [June 29, 1977]). We do find, however, that applicant has satisfied the requisites of *Dayton Power and Light Company*, Case No. 79-372-GA-AIR (May 7, 1980), with respect to its proposed annualization of overtime expense, and that adjustment should be approved. Pension costs will be adjusted to reflect the above findings.

**Power Plant Maintenance Normalization:**

The applicant and the staff both adjusted power plant maintenance expenses to reflect the deferral of maintenance originally scheduled for the first half of the test year to future periods due to the extended shut-down of Davis-Besse during the second quarter of 1979 (App. Ex. 1, Sched. C-3.11; S.R., p. 14; S.R., Sched. 3.12). The staff adjustment normalized maintenance only to the extent budgeted maintenance was pushed into the second half of the test year. Applicant's adjustment recognized maintenance deferred into 1980. The purpose of this adjustment is to establish a reasonable annual allowance for

power plant maintenance. The Commission agrees with applicant that the staff adjustment fails to recognize the level of maintenance which would have been performed during the test year but for the unusual outage. The deferral of maintenance for the first half to the second half of the year meant that maintenance planned for the latter period had to be deferred until some subsequent time as maintenance schedules had become filled (App. Ex. 5A, pp. 22-24). Applicant's adjustment should be approved and its objection to the staff adjustment is, hereby, sustained.

**Vehicle Fuel Annualization:**

In recognition of the extraordinary increases in the cost of fuel used in company vehicles, the staff annualized vehicle fuel prices to year-end levels (S.R., Sched. 3.7). Applicant also proposes an annualizing adjustment to vehicle fuel; but would have the Commission calculate the adjustment with reference to March, 1980 price levels (App. Ex. 1, Rev. Sched. C-3.8; App. Ex. 5A, p. 21). Our earlier discussion with respect to annualizations based on post-test year data is dispositive of this issue as well. The Commission is, of course, aware that gasoline prices have continued to rise after the close of the test year. However, an annualization based on some post-test year price level ignores what the company's response to this post-test year increase might be. The matching principle may be violated. For example, in this instance applicant's witness Chopp acknowledged that the company was undertaking programs to reduce fuel consumption in an effort to offset these increased costs (Tr. II, p. 110). One would not reasonably anticipate that even the company's most stringent conservation program would totally offset the rise in prices; but the point is that there is no way to measure what the actual effects may be. Thus, although the cost

change may be known and measurable, an element of speculation remains. The Commission overrules applicant's objection to the staff's adjustment.

**Storm Damage and Tree Trimming Expense:**

As in applicant's prior case, the staff normalized storm damage and tree trimming expense to assure that the rates set in these proceedings would reflect a representative allowance for these items (S.R., p. 14; Staff Ex. 3, Rev. Sched. 3.13 and 3.14). The staff method, which was essentially the same as that approved in the last case, was based on an average of the annual expenses incurred for these items for the previous five years, restated to 1979 dollars. Applicant objected to the staff adjustments and offered alternative calculations based on essentially the same method rejected in the last case. Applicant contends that the staff's adjustment fails to recognize that there has been an actual increase in the amount of work being done; but the company has offered little in the way of conclusive proof that this alleged increase has, in fact, occurred (Staff Reply Brief, p. 14). Consistent with our decision in applicant's prior case, the Commission again finds the staff adjustments to be proper.

**Ordered Load Research Expenses:**

Applicant proposed an adjustment to test-year expenses to reflect costs associated with load research activity it is compelled to engage in under the provisions of the Public Regulatory Policies Act of 1978 (App. Ex. 1, Sched. C-3.10). The staff recommends that this adjustment be rejected (S.R., p. 18). This expense of $72,084 relates to certain load meters which applicant leased after the close of the test year. The staff's opposition to the adjustment is based not only on the fact that no costs were incurred in the test year, but also on its observation that while the transaction is treated as a lease for purposes of this adjust-

ment, it will be treated as a purchase and capitalized when the property is actually acquired (S.R., p. 14). The Commission agrees that the adjustment should be disallowed.

**Advertising Expense:**

The staff reviewed the advertising expenses included in applicant's test-year operating expenses and concluded that no adjustment was required based on its view that the company's advertisements conformed to Commission guidelines and PURPA standards (S.R., p. 15). However, at hearing, Consumers' Counsel and Senior Citizens, *et al.*, presented a series of exhibits which contained the copy of advertisements placed in various media by the Illuminating Company during the test year (O.C.C. Ex. 6; Senior Citizens Ex. 11). These adds are clearly promotional and of no benefit to the consumers. In general, the only information they impart is a general observation that although the cost of service has risen over the years, electricity still represents a good value. As calculated from exhibits indicating the test-year expense associated with these ads, their jurisdictional cost was $238,617 (O.C.C. Ex. 7, Senior Citizens Ex. 12). This amount should be eliminated from allowable expenses. The Commission can anticipate applicant's objection to this adjustment. It will be based on the argument that no witness offered testimony that the advertising was promotional in nature or did not benefit consumers. Our response will be borrowed from another source. We know it when we see it.

**Charitable Contributions:**

As fully explained in the Commission's decision in the company's last rate case, the Illuminating Company does not generally contribute directly to charity, but makes its donations through the vehicle of the CEI Foundation. However, in the course of its investigation the staff did discover some $18,352 that the company had charged to

jurisdictional operation and maintenance expense which the staff believed should be reclassified as a charitable contribution (S.R., p. 15; S.R., Rev. Sched. 3.17). Applicant explained that it had elected to treat this amount as an expense for fear that if it made the donations through the CEI Foundation it could be subjected to penalties if the IRS perceived an indirect benefit to the company (App. Ex. 5A, p. 25; Tr. II, p. 115). The Commission is not particularly concerned as to what treatment the company accords this amount for tax purposes; but for ratemaking purposes it is clear that it should be considered as a charitable contribution. Applicant's objection to the reclassification is overruled.

This Commission has consistently approved a reasonable allowance for charitable contributions in its cost of service analyses and was prepared to do so again in these proceedings. However, the opinion just issued by the Supreme Court in *City of Cleveland v. Public Utilities Commission*, S.Ct. Case Nos. 79-1158 and 79-1173 (July 9, 1980), 63 Ohio St. 2d(1980), quite clearly reverses the Court's recent decision in *City of Cincinnati v. Public Utilities Commission*, 55 Ohio St. 2d 168 (1978), which specifically approved this long-standing Commission practice. In accordance with this new decision, the Commission now finds that the intervenors' objections to any allowance for charitable contributions should be sustained. As the Commission would have accepted the staff's method of calculating an allowance for charitable contributions as we did in the prior case, the effect is to reduce allowable expenses from what we would have otherwise determined by the amount of $492,539 (S.R., Sched. 3.18).

**Rate Case Expense:**

Contrary to customary practice, the company did not propose an allowance for expenses incurred in connection with these proceedings in its cost of service analysis.

Rather, applicant elected to rely on the rate case expenses actually charged to its books during the test year on the theory that it will be filing such cases on an annual basis (App. Ex. 5A, pp. 26-27). The staff did obtain an estimate of the costs anticipated by applicant in connection with these proceedings (App. Ex. 1, Sched. C-9), made a determination that the estimate was reasonable, and recommended that the estimated expense be amortized over a two-year period. Thus, the staff's proposed allowance is $174,000 (S.R., Sched. 3.19). Upon review of the record relative to this subject, the Commission believes the staff's proposed allowance should be accepted. The bulk of the rate case expense incurred by applicant during the test year related to its prior case. As a theoretical matter, expenses associated with the prior case should not be built into the rates authorized in these proceedings. Moreover, the Commission is concerned that applicant's proposed method of dealing with this subject may make our review of the reasonableness of these expenditures more difficult. With due regard for our prior observations concerning the nature and purpose of the rate case expense allowance, the Commission sees no reason to depart from our usual practice with respect to this item (See, *e.g., Columbus and Southern Ohio Electric Company,* Case No. 77-545-EL-AIR [March 31, 1978]).

Intervenor City of Cleveland objects to the staff's proposed allowance for rate case expense and a considerable portion of this record is devoted to its attack on the reasonableness of the staff's finding. This onslaught was then broadened to include the question of legal fees in general. Despite the pages of transcript generated by the City of Cleveland's efforts in this regard, there is not one iota of affirmative evidence that the rate case expense allowance is unreasonable or that applicant's practices with respect to retaining legal counsel are inconsistent with that which should be expected from a major corporation

(Tr. XXXI). Further, intervenor never suggested, either through a witness or on brief, what it considered to be reasonable with respect to these areas. All the Commission is left with are its bare assertions that the amounts proposed by the applicant and the staff are not. These objections should be overruled.

**PUCO Maintenance Tax and Consumers' Counsel Assessment:**

Although it has been the consistent practice of the Commission, applicant objects to the staff's classification of the PUCO maintenance tax and Consumers' Counsel assessment as "other taxes", contending that the Uniform System of Accounts requires that they be charged to operation and maintenance expense (App. Ex. 5A, p. 24). The significance of this issue is, of course, the effect on the working capital calculation. On brief, staff counsel argues that the accounting requirements are not as clear cut as applicant would have us believe and points out that applicant is one of the few utilities that does not account for these items as taxes (Staff Reply Brief, p. 11). Neither of these arguments need detain us, for no matter what method the company elects to employ for bookkeeping purposes, the Commission would still consider the assessments as taxes for ratemaking purposes. Applicant's objection to the staff's classification is overruled, as is its objection that these amounts should be allocated, a matter decided in the company's last case.

**Pennsylvania Public Utility Realty Tax (PURTA):**

Pennsylvania has enacted a public utility realty tax which significantly increased applicant's tax obligation in that state commencing with the 1979 tax year. As a part of this new law, the Pennsylvania legislature also imposed a one-time surcharge, in applicant's case amounting to approximately $1.4 million, which the company paid dur-

ing the test year. Although both the applicant and the staff recognized the PURTA tax in their calculation of allowable expenses, the staff eliminated the surcharge payment from its cost of service determination (S.R., p. 17; S.R., Sched. 3.24e). Applicant objects to the staff adjustment.

The Commission has had occasion to consider this precise question in its recent decisions in *Ohio Edison Company*, Case No. 78-1567-EL-AIR (January 30, 1980) and *Toledo Edison Company*, Case No. 79-143-EL-AIR (February 29, 1980). Consistent with those decisions, the Commission again concludes that the staff adjustment is, in all respects, reasonable and proper and should be approved. No one disputes that this one-time surcharge is a nonrecurring expense. As such, it should not be reflected in future rates, and applicant's now familiar arguments to the contrary must, accordingly, be rejected. There is no merit in the claim that this nonrecurring expense should be allowed in recognition of the possibility that there may be other nonrecurring expenses in the future, nor is their merit in the theory that disallowing the expense will encourage state legislatures to view the mechanism of a surtax as a source of "free money" (App. Ex. 5A, pp. 30-32). The risk that there will be unanticipated expenses in the future is a risk assumed by the investor when he purchases the company's securities. Indeed, the investor's assessment of this risk plays a big part in establishing his return requirements. Further, a state legislature which intentionally pursued the course hypothesized by applicant would either effectively render what was nominally a one-time surcharge a recurring expense deserving of rate recognition, or would create a climate which would ultimately result in increased investor requirements relative to the affected utilities. Those increased requirements would, in time, lead to increased rates.

On brief, applicant submits that its property "is simply confiscated" by the exclusion of this item from cost of service (App. Brief, p. 16). This is nonsense. As this Com-

mission has repeatedly pointed out, the purpose of rate regulation is not to guarantee the dollar-for-dollar recovery of specific past expenses, but rather to determine a representative allowance for expenses which will provide a reasonable future earnings opportunity (See *e.g., Ohio Edison Company,* Case No. 77-1249-EL-AIR [November 17, 1978]). Applicant suggests that the Pennsylvania legislature imposed this surcharge in order to retain monies collected during the pendency of a challenge to an earlier version of the PURTA tax which eventually resulted in the tax being overturned. (See *Commonwealth v. Philadelphia Electric Co.,* 472 Pa. 530 [1977]). This points up the very reason nonrecurring costs are not considered in fixing future rates. Assume for purposes of discussion that the court decision had been adverse to utility interests and that the tax had not theretofore been considered for ratemaking purposes. The fact that applicant loses sight of in its "confiscation" argument is that building a mechanism for recovery of the surcharge into future rates would have absolutely no effect on the company's 1979 financial performance. The Commission has not denied applicant an earning's opportunity. The expense is history and has no place in the establishment of future rates.

**Federal Income Tax:**

Through its filed objections, applicant originally took exception to a number of aspects of the staff's federal income tax calculation. Most of these objections were tied to other staff expense adjustments and are now resolved. Of those that remain, applicant pursued only the investment tax credit amortization question on brief. The treatment the staff accorded this item is in keeping with that approved in prior Commission cases, and is the balance of the staff's method. The staff's calculation of federal income tax expense should be accepted for purposes of these proceedings.

**Terminated Generating Units:**

By an amendment to its original application, applicant seeks Commission approval of an adjustment to allowable expenses which would permit the company to recover its share of the costs associated with the termination of four nuclear generating units pursuant to the CAPCO decision of January 23, 1980, that Davis-Besse No. 2 and No. 3 and Erie Nuclear Unit No. 1 and No. 2 should be cancelled. Applicant's specific proposal is that the expenses incurred to date for these projects, $56,437,000, be adjusted to reflect necessary tax considerations and amortized over a ten-year period (App. Ex. 4A, p. 22; App. Ex. 1, Sched. 3.22). The staff recommends approval of the adjustment (Staff Ex. 11, pp. 18-20; Staff Ex. 7, pp. 37-40). Consumers' Counsel and intervenors City of Cleveland and Senior Citizens, *et al.*, object to any recognition of these termination costs in the rates to be established in these proceedings.

As a preliminary matter, the Commission must first take up intervenors' claim that this issue is not properly before the Commission as the adjustment was not proposed until after the notice of the rate request required by Section 4909.18 Revised Code had been published. The Commission disagrees with these arguments, noting that statute only contains the requirement that "the substance of the application" be noticed. Because applicant did not propose any specific increase in the actual rates requested, the substance of the application is unaffected by this later adjustment to the supporting data. Had the proposal predated the notice, there would certainly have been no requirement that it be included in the publication.

The real threshold question here, which the Commission perceives as the most difficult of all the issues raised in connection with this matter, is whether this adjustment is legally permissible. In reviewing all the available cases considering cancellation costs from both state and federal

regulatory jurisdictions, we find the most surprising feature to be, not the fact adjustments of this type have been approved without exception, but that there is no hint that this legal question was ever even raised (App. Ex. 4A, p. 69). At first blush, one would think that the risks of cancellation should be borne solely by the investor; however, applicant's arguments persuade us that this is not the case (App. Brief, pp. 8-15). Intervenors approach this issue as though it were a rate base question, emphasizing the fact that the terminated units have never and will never provide service to customers. This is quite clearly correct, but it is irrelevant. There is no request by the company that it be permitted to earn a return on this investment, although some jurisdictions have permitted this treatment. What the company seeks is the recovery of costs incurred on behalf of its ratepayers to assure that adequate service could be maintained (Tr. XXI, p. 185). The significant question, given the Commission's past pronouncements with respect to the impropriety of the recovery of past losses through future rates, is whether the amortization of these extraordinary costs does violence to this principle. The distinguishing feature that sets this adjustment apart from those we have rejected on this ground in the past is that costs associated with the termination of the units did not really become costs until the fact of termination. Cancellation does not create a past loss, but gives rise to a current cost. Unlike the PURTA surtax issue discussed earlier, where approval of the proposed adjustment would have had no effect on the company's future earnings opportunity, rejection of this adjustment would have a very direct impact on applicant's financial performance as, in the absence of funding of the amortization through rates, applicant would be required to write off these costs currently (Tr. XXII, p. 49). Thus, we now see the wisdom of the standard emerging from the cases from other jurisdictions; if the expenditures are prudent, amortization should be permitted.

In determining whether these expenditures were prudent, one must bear in mind what is and what is not at issue. No one disputes that the 1973 decision to embark on the construction in question was reasonable as it was based on the best data available (App. Ex. 11; App. Ex. 29; Staff Ex. 11). Similarly, no one disputes that the decision to terminate construction was reasonable, given the intervening decline in growth expectations and the uncertainties which now attend the construction of nuclear units. Thus, the only real question is whether the decision to terminate should have been made sooner. Applicant's witness William described in detail the company's response to changes in growth rates, including postponements of units so that in-service dates would better match the results of new load forecasts (App. Ex. 11, p. 30). Only Consumers' Counsel witness Rosen offered testimony suggesting that the units should have been cancelled earlier (O.C.C. Ex. 5), and his opinion is of doubtful value as it is based solely on CAPCO information and does not specifically address any of the considerations which may have influenced this applicant's decisions (Tr. XXVIII, p. 115; Tr. XXIX, pp. 19-21). Further, the alternative construction program he now recommends for CAPCO, which involves an unbelievable reliance on oil-fired peaking units, casts doubt on the credibility of his entire study, even if it were found to have any application in this case. The Commission finds that applicant's decisions were reasonable and prudent at every step of this process, and concludes that the proposed adjustment should be approved. For purposes of these proceedings we accept the staff's method of calculating the adjustment (Staff Ex. 3; Sched. 3.0).

**Operating Income Summary:**

Consistent with the foregoing discussion, the Commission finds applicant's jurisdictional adjusted operating income for the twelve months ending December 31, 1979,

the test period in these proceedings, to be as set forth on the schedule below. Although revenues can be directly assigned to the application area or the City of Cleveland, expenses must be allocated. The following schedule also depicts the results of the application of the staff's proposed expense allocation factors which the Commission has accepted as reasonable for purposes of these proceedings:

**Adjusted Operating Income**
**(000's Omitted)**

| | Total Jurisdiction | Application Area | City of Cleveland |
|---|---|---|---|
| **Operating Revenues** | $773,389 | $542,489 | $230,900 |
| **Operating Expenses** | | | |
| Operation and Maintenance | $471,852 | $330,775 | $141,077 |
| Depreciation Expense | 61,277 | 43,342 | 17,935 |
| Taxes Other Than FIT | 76,194 | 53,163 | 23,031 |
| Federal Income Tax | 39,355 | 28,227 | 11,128 |
| **Total Operating Expenses** | $648,678 | $455,507 | $193,171 |
| **Net Operating Income** | $124,711 | $ 86,982 | $ 37,729 |

## PROPOSED INCREASE

A comparison of jurisdictional operating revenues of $773,389,000 with the allowable jurisdictional expenses of $648,678,000 indicates that under its present permanent rates applicant realized income available for fixed charges in the amount of $124,711,000 based on adjusted test-year operations. Applying this dollar return to the jurisdictional rate base of $1,485,734 results in a rate of return under present rates of 8.39 percent. Current rates to customers in the application area produced test-year income available of $86,982,000, which, when applied to the allocated rate base of $1,030,866, yields a rate of return of 8.44 percent. Present rates to customers in the City of Cleveland, which

are the same as those contained in the ordinance complained of, resulted in adjusted test-year net operating income of $37,729,000. This dollar return, when applied to the rate base properly allocable to the City of Cleveland of $454,868,000, produces a rate of return of 8.29 percent. All these rates of return are well below that recommended as reasonable by any of the expert witnesses testifying on this subject and the Commission must, therefore, find that the company's present rates are insufficient to provide it reasonable compensation and return for the electric service it renders. Moreover, Ordinance No. 1673-79 of the City of Cleveland, which would continue these rates in effect in that municipality, must also be found to be unreasonable. Rate relief is clearly required, and the ordinance complained of must be modified.

Under the rates proposed by applicant, additional gross annual revenues of $79,795,000 would have been realized based on test-year operations as analyzed herein (S.R., Sched. 1). On a pro forma basis, which assumes necessary expense adjustments calculated in a manner consistent with the Commission's findings, this proposed increase would have yielded an increase in jurisdictional net operating income of $41,301,000 resulting in income available for fixed charges of $166,012,000. Applying this dollar return to the jurisdictional rate base results in a rate of return of 11.17 percent. Net operating income for the application area would be increased to $116,008,000 under the proposed rates, resulting in a rate of return on the rate base allocated to this service of 11.25 percent. For the City of Cleveland, the proposed increase produces pro forma income available of $50,004,000 and a rate of return on rate base of 10.99 percent. Although these rates of return are supported by the opinions of applicant's rate of return witnesses, the jurisdictional rate of return under the proposed rates is above the range recommended as reasonable by the staff witness testifying on this subject. The existing rates

are inadequate; but further examination is necessary before a final determination as to the level of rate relief required can be made.

## RATE OF RETURN

Three witnesses offered cost of capital analyses to be considered as evidence by the Commission in establishing a fair rate of return for purposes of these proceedings. The study sponsored by applicant's witness Jeffries concludes that a rate of return of from 11.17 to 11.55 percent is appropriate (App. Ex. 8A, p. 8), and applicant's witness Maugans proposes a nearly identical range (App. Ex. 4A, p. 64). Witness Farrar, testifying on behalf of the staff, determined the overall cost of capital to be between 10.65 and 11.02 percent (Tr. XXIV, pp. 4-5). Although the difference between the company and staff positions lies primarily in the area of the cost of common equity, there are certain other minor issues which the Commission must first address.

### Capital Structure:

Each of the witnesses employed the company's December 31, 1979, capital structure in their respective cost of capital analyses. The use of a capital structure which reflects post-date certain developments has been approved by the Commission in a number of recent decisions in an effort to better recognize the cost of capital to the applicant utility which will prevail in the period for which rates are being set. (See, *e.g.*, *Dayton Power and Light Company*, Case No. 78-92-EL-AIR [March 9, 1979] and *Ohio Edison Company*, Case No. 78-1567-EL-AIR [January 30, 1980]). Consistent with those decisions, the Commission finds the use of the December 31, 1979, capital structure to be appropriate. The specific ratios, as calculated by Mr. Farrar, are 46.57 percent long-term debt, 15.01 percent preferred stock, and 38.41 percent common equity (Staff Ex. 11,

p. 21). These percentages differ slightly from those computed by applicant due to the fact that the staff and the applicant used different techniques to adjust for a loss experienced by the company in connection with a reacquisition of preferred stock in 1978 (Staff Ex. 11, p. 3). As applicant acknowledges on brief, the difference in the result is not significant (App. Brief, p. 35). Accordingly, we accept the capital structure proposed by Mr. Farrar as reasonable for purposes of these proceedings.*

**Cost of Debt and Preferred Stock:**

Each of the rate of return witnesses testifying in these proceedings derived the costs to be assigned the debt and preferred stock components of applicant's capital structure by reference to the actual embedded costs of these senior securities. Despite the fact that its own expert witness specifically testified to the contrary (Tr. XVII, pp. 72-73), applicant continues to suggest, as it did in its filed objections, that the use of embedded costs for this purpose is unreasonable and unlawful (App. Brief, p. 35). Although we agree with applicant that a determination of this issue is certainly not essential in this case, the Commission believes it appropriate to lay this theory to rest at this time.

Section 4909.15(D)(2)(a) Revised Code now requires that the Commission determine a fair and reasonable rate of return for an applicant utility with reference to the

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* Although he presented no independent rate of return recommendation, Consumers' Counsel witness Larkin suggested that the Commission should recognize short-term debt in the capital structure utilized in the cost of capital analysis (O.C.C. Ex. 2, pp. 5-8). Such a step would be inconsistent with Commission precedent and contrary to the specific recommendations of the other witnesses; however, the Commission need not reach this question as Consumers' Counsel has, on brief, now indicated its support of the use of the staff's capital structure for purposes of these proceedings (O.C.C. Brief, p. 4).

embedded cost of debt of the utility in question. As anyone familiar with the 1976 changes in Ohio's ratemaking statutes can attest (Am. Sub. S.B. 94), this provision was inserted in response to the decision of the Supreme Court of Ohio in *Cleveland Electric Illuminating Company v. Public Utilities Commission*, 42 Ohio St. 2d 403 (1975), wherein the Court apparently held that the then-existing statutory framework required that the Commission employ the current cost of debt in its rate of return determination. However, even before the legislative reversal of the *Cleveland Electric Illuminating Company* decision, *supra*, the Commission, in its Entry on Rehearing in *Cincinnati Gas and Electric Company*, Case No. 72-415-Y (October 17, 1975), undertook a careful analysis of the existing precedent which let it to the unanimous conclusion that the use of embedded costs was both theoretically appropriate and legally permissible. We commend this discussion to applicant's attention and point out that its logic is even more compelling now that Ohio rate regulation no longer even arguably involves the fictional reproduction of rate base at date certain.

Applicant contends that even if Section 4909.15(D)(2)(a) Revised Code now specifically requires consideration of the embedded cost of debt in the rate of return determination, the silence of the statute with respect to preferred stock should be construed as evidence of a legislative intent that current costs be employed in connection with this capital component. Although the Commission does not take issue with the principle of construction cited by applicant, the result produced by its application in this setting is so unreasonable that we do not believe it can logically be invoked. As suggested above, a review of the history of this provision clearly indicates that it was enacted to overturn a specific judicial decision, not as a directive to the Commission to alter its consistent practice of relying on embedded costs as the best evidence of the

appropriate cost rates to be assigned the long-term debt and preferred stock components of the capital structure. The Commission's discussion of the embedded cost question in *Cincinnati Gas and Electric Company, supra,* in dispositive of this issue as well. Even in the days of the RCNLD rate base, it was a rare exception when a utility rate of return expert proposed the use of anything other than embedded costs in his determination of the weighted cost of senior securities; and the Commission has certainly never been treated to testimony exclusively advocating current costs for these capital components since Ohio became an original cost jurisdiction.

As indicated above, the Commission has accepted the capital structure proposed by staff witness Farrar. We now further find Mr. Farrar's determination of the embedded cost of debt, 8.19 percent, and preferred stock, 8.30 percent, to be reasonable and adopt same for purposes of the analysis in these proceedings (Staff Ex. 11, p. 3).

**Cost of Common Equity:**

Determining the cost of debt and preferred stock is, and as explained above, should be largely a mechanical process. The cost of common equity, however, can only be estimated. As the Commission has noted on a number of prior occasions, a variety of valid methods exist for obtaining this estimate, and the fact that the Commission selects the recommendation of one witness over that of another does not mean that any of the recommendations are "wrong," save in those instances where internal inconsistencies render a particular recommendation unacceptable even under the sponsoring witness's own approach. The Commission must, in a necessary exercise of its judgment, select that recommendation it believes to be most reasonable in light of the facts and circumstances of a given case. This task is made even more difficult in this case due to the radical changes in financial conditions experienced from the outset

of the test year through the present time. Indeed, these changed circumstances have prompted each of the witnesses offering testimony on the cost of equity to revise his recommendation.

In his original testimony, filed in September of 1979, applicant's witness Jeffries recommended a return on common equity of from 15.0 to 16.0 percent (App. Ex. 8, p. 30). The range he proposes in the supplemental testimony submitted just prior to hearing is 16.00 to 17.00 percent (App. Ex. 8A, p. 2). Applicant's witness Maugans originally suggested as reasonable a rate of 15.5 percent (App. Ex. 4, p. 70). He now supports Mr. Jeffries' revised recommendation (App. 4A, p. 1). As set forth in the staff report, the staff's original position was that the appropriate cost of equity was in the range of 14.01 to 14.94 percent (S.R., p. 27). At hearing, witness Farrar adjusted this recommendation to reflect more current data and concluded the proper cost of equity was between 14.56 and 15.52 percent (Tr. XXIV, pp. 4-5).

Mr. Jeffries employed several methods in arriving at his original recommendation. He performed a comparable earnings test involving a review of the return on common equity achieved over the past ten years by sixteen electric utilities with bond ratings the same as that of the applicant (App. Ex. 8, pp. 20-21; App. Ex. 8, p. 6; Tr. XVII, p. 29). Based on this analysis, Mr. Jeffries concluded that a rate of return on common of 15.00 percent would be appropriate. In evaluating this recommendation, the Commission observes that at no time in the past ten years has the average return of the sixteen companies studied ever reached 15.00 percent. In fact, in the years since 1974, the year of the oil embargo and general business recession, the achieved return for this group has been well below this figure. In both 1978 and 1979 it was 13.2 percent. Mr. Jeffries explained that in arriving at his recommended return based on this evidence he gave consideration to

recently granted and pending rate increase requests (App. Ex. 8, p. 20); however, the effect of these increases was never quantified.

The disparity between the actual data and the witness' recommendation based on that data is not surprising. Indeed, this discrepancy highlights one of the shortcomings of the comparable earnings method which the Commission has identified in the past (*Columbus and Southern Ohio Electric Company,* Case No. 77-545-EL-AIR [March 31, 1978]). Where the members of the group examined for comparative purposes exhibit depressed market-to-book ratios, a vicious circle will be created if their achieved returns are relied on by regulators in determining the rate of return to be authorized in a given case. On the other hand, the logic of the method breaks down if one first looks to the experience of the group defined as comparable, concludes that the experience is not really suitable as evidence under existing conditions, and then, through an exercise of judgment, attempts to establish a return requirement based on a perception of what the group should be earning. This is not to say that the Commission should totally discount the experience of other comparably-rated electric utilities, but merely to point up the fact that the witness has used a good deal of judgment in deriving an equity return recommendation of 15.00 percent from data which, on its face, would apparently support a much lower number.

Mr. Jeffries also looked to the rate of return on common equity of Standard & Poor's 400 Industrials over the past ten years as a basis for his recommendation (App. Ex. 8, p. 21; App. Ex. 8, p. 30; App. Ex. 8, p. 39). He concluded from an examination of the average return earned by this group in the years 1976 through 1978 that a range of 14.50 to 15.20 percent could be supported, and also indicated that in 1979 the experienced return had jumped to 16.90 percent (Tr. XVII, p. 36). The witness included this broad

industrial composite on the theory that the member companies represent alternative investment opportunities and that applicant must compete for funds with these firms in the money market. Although this evidence may be of some value from the standpoint of providing a broad overview, the Commission does not believe it appropriate to predicate a return recommendation on the experience of this large, diverse group, particularly without any detailed analysis of the characteristics of its members. The cornerstone of the alternative opportunity cost concept upon which the comparable earnings method is based is that the return authorized should be commensurate with returns being earned on investments in other business undertakings having similar or corresponding risks, but should not be so high as the returns which might be realized from highly profitable enterprises or speculative ventures. *Bluefield Waterworks Company v. Public Service Commission*, 262 U.S. 679 (1923). Thus, there must be a showing that the enterprises selected for comparative purposes are, in fact, comparable. There has been no such showing in this case, and the Commission can accord little weight to a return recommendation based on this data.

A comparable earnings approach was also employed by Mr. Jeffries in connection with his efforts to emphasize the importance of fixing a rate of return on common equity which will allow the company to attract capital on the most reasonable terms possible (App. Ex. 8, p. 24). Although applicant's bonds are still rated double-A by Moody's, they have been recently downgraded by Standard and Poor's to AA- (App. Ex. 8, p. 24). The company lost its double-A preferred stock rating in 1976 (App. Ex. 8, p. 28). As an improvement in the current ratings would result in lower financing costs to the company, the witness deemed it appropriate in recommending a rate of return on equity to evaluate the achieved return of electric utilities with double-A ratings for both preferred stock and bonds (App. Ex. 8, p. 43). This reduced the number in

the original group studied from sixteen to twelve. The resulting average return is slightly higher during the years since 1974 than the average return for the larger sample, with the exception of 1979 when it was actually lower. In no event, however, did this average return approach 15.0 percent, the lower bound of the witness' equity return recommendation. There is no need to repeat our earlier comments with respect to the inherent problems in the comparable earnings approach, but an additional observation is in order. There is much more involved in solidifying or improving applicant's present ratings than merely handing out rate increases, as company witness Maugans acknowledged (Tr. X, pp. 54-68; Tr. XII, pp. 164-166). Adequate rate relief is an important step, but utility management also has a definite role to play as it is the company's performance over time that influences the rating agencies. The Commission recognizes that improved ratings will lead to lower future financing costs, but the real question is what price we should ask the consumers to pay presently for this future benefit. This is the very heart of the rate of return inquiry, and a balance must be struck. Were it not for this consideration, we could simply send the rate of return witnesses home and decide the earnings requirement question solely through an analysis of coverage ratios. There is quite clearly more to establishing a reasonable earnings opportunity than a mechanical calculation designed to satisfy the rating agencies' coverage tests.

As a fourth measure of the appropriate return on common equity, Mr. Jeffries performed a risk premium analysis involving a comparison of the yield on new double-A rated utility bonds with the return on equity of double-A rated electrics for the years 1964 to 1978. The average equity-debt risk spread for the period was 5.91 percent (App. Ex. 8, p. 43). He then applied this risk spread to the average yield on newly issued bonds of similar rating for the twelve months ended August, 1979, which he calcu-

lated to be 9.6 percent (App. Ex. 8, p. 29). Summing the two numbers produced an indicated return on common equity of 15.51 percent. Staff witness Farrar, who also performed a risk premium analysis as a check on the reasonableness of his own cost of equity recommendation (S.R. 29, pp. 29-30), criticized Mr. Jeffries' use of achieved returns on common equity for purposes of establishing the annual differential (Staff Ex. 11, pp. 11-12). He argued that the use of achieved returns is improper as achieved returns do not necessarily reflect the actual cost of equity. The Commission notes that in the earlier years of the study, where the annual differential was the greatest, utility stocks were commonly sold above book value. This certainly lends support to Mr. Farrar's contention that the average risk spread employed by Mr. Jeffries is too high. However, even based on Mr. Jeffries' own method of calculation, we observe that the annual differential reached the average for the period only once in the 1970's and that was in 1972. If one limits the historical time frame of the analysis to what is clearly a more representative period in terms of future expectations, say 1975 through 1978, one gets far different results. Using Mr. Jeffries' numbers, the average equity-debt risk spread for the more recent period is 3.74 percentage points. Combining this risk premium with the 9.6 percent referred to above produces an indicated rate of return on common equity of 13.34 percent, a far cry from the 15.51 percent derived by Mr. Jeffries through his methodology but an extraordinarily good match with the 1979 data utilized in his comparable earnings test. Moreover, a risk differential of 3.74 percentage points exceeds that determined by Mr. Farrar who, it will be remembered, based his calculation on an estimate of the cost of equity rather than the realized return on equity. This effectively answers the charge that the risk premiums is understated during more recent years due to insufficient achieved returns (App. Ex. 8, p. 29).

Mr. Farrar had the benefit of final figures for calendar 1979 at the time he performed his original analysis (S.R., p. 30). At hearing, Mr. Jeffries updated his calculation of the average monthly yield on new double-A rated utility bonds to take into account the balance of the test year. His determination of the yield, 10.48 percent, exceeds slightly that calculated by Mr. Farrar as he limited his study to new issues. However, if we accept Mr. Jeffries number for the purpose at hand, and combine 10.48 percent with a risk premium of 3.74, the indicated return on common equity becomes 14.22 percent. Again, this is well below the witness's recommended range, but does fall well within the bounds of the staff witness's original recommendation.

The final method employed by Mr. Jeffries in arriving at his original recommended cost of equity was what he characterized as a "market based" approach (App. Ex. 8, pp. 22-23). Indeed, this is a version of the discounted cash flow analysis (DCF) familiar to the Commission and consistently approved by it in the past as an appropriate means of measuring investor expectations. Under his application of the method, Mr. Jeffries concluded that the base line cost of equity was 14.50 percent. He then adjusted this cost by 10 percent to recognize issuance costs, market pressure, and dilution (App. Ex. 8, p. 23). This produced a recommended return on equity of 15.95 percent.

Staff witness Farrar also based his cost of equity recommendation on a DCF analysis. As detailed in the staff report, he determined the base line cost of equity to be 13.58 percent (S.R., pp. 28-29). Applying the staff's customary adjustment factors of 1.032 and 1.10 to this base line costs resulted in an indicated cost of equity of from 14.01 to 14.94 percent.

Given our reservations with respect to the conclusions drawn by Mr. Jeffries from the other methods he employed, it is apparent that our decision as to the appropri-

ate return on equity comes down to a choice between Mr. Jeffries' and Mr. Farrar's DCF recommendations. Although applicant's witness Maugans also initially offered a cost of equity recommendation, his supplemental testimony relating to this area is largely devoted to a criticism of Mr. Farrar's analysis, and specifically accepts as fair the revised recommendation of Mr. Jeffries (App. Ex. 4A, p. 1). In light of this development, the Commission sees no purpose to be served by picking our way through Mr. Maugans' original proposal. We would note, however, that the testimony of Mr. Farrar raised significant questions as to the reasonableness of his methods (Staff Ex. 11, pp. 12-14).

Before considering the specifics of the competing positions of the applicant and the staff as to the proper application of the DCF formula for purposes of these proceedings, the Commission feels compelled to address certain charges contained in applicant's brief relative to the Commission's reliance on this method. Applicant apparently entertains the suspicion that the Commission's preference for the DCF approach is based on a belief that it is less subject to the vicissitudes of an individual witness's judgment than are other recognized methods (App. Brief, p. 36). This is simply not true. The Commission's general acceptance of DCF-based equity cost recommendations is grounded in the fact that DCF, by design, is a market measure of investor requirements, the very factor which must be isolated in determining the cost to the company of equity capital. The Commission has never intended to suggest that the application of the DCF formula is a mechanical process, as a review of our recent orders relative to this subject will bear out. (See, *e.g.*, *Cincinnati Gas and Electric Company*, Case No. 79-11-EL-AIR [January 7, 1980]; *Toledo Edison Company*, Case No. 79-143-EL-AIR [February 29, 1980]). Moreover, although the Commission has relied heavily on the DCF method in

the past, we have never intended to suggest that it is the only acceptable method for determining the cost of equity capital.

The DCF method is based on the premise that the cost of equity capital is equal to the sum of the current dividend yield and the rate of growth in dividends (S.R., pp. 47-50). Dividend yield is, of course, determined by dividing the common stock dividend by the price. Mr. Jeffries, who for purposes of his original testimony was limited to data available through August, 1979, calculated dividend yield to be 10.5 percent based on a dividend of $1.92 per share and an average market price of applicant's common stock of $18.25 for the then most recent twelve month period (App. Ex. 8, p. 22). Mr. Farrar, who had calendar 1979 data available at the time of his original study, determined the yield to be 11.33 percent based on a $2.00 dividend and a twelve-month average price of $17.65 (S.R., p. 29). Thus, the methods for determining yield were identical, both witnesses specifically agreeing that the use of a twelve-month average price was appropriate (App. Ex. 8, p. 22; Staff Ex. 11, p. 14). We will defer consideration of applicant's apparent change in position with respect to this component of the formula for our discussion of the revised recommendations of the witnesses.

The critical difference in the DCF methodology as applied by Mr. Jeffries and Mr. Farrar lies in their respective estimates of the proper value of the growth component of the formula. Mr. Jeffries estimated growth by computing annual growth rates for common stock book value, earnings per share, and dividends for the period 1968 through 1978: 4.7 percent, 3.2 percent, and 3.6 percent, respectively (App. Ex. 8, p. 41). He then assumed that earnings growth should receive less weighting than the other two elements when forming a judgment with respect to a future growth rate, and concluded that a 4.0

percent growth factor was reasonable (App. Ex. 8, p. 23). Mr. Farrar, on the other hand, estimated growth by use of the "b x r" approach, "b" equalling the retention rate of earnings, and "r", the earnings on the common equity funds retained (S.R., p. 29). Based on his review of the results of the "b x r" calculation for several different periods, his observations concerning the relationship between earnings and dividend growth, and the inferences he drew from the recent increase in yield of the company's common stock, he recommends a 2.25 per cent growth factor.

Applicant's witness Maugans was highly critical of Mr. Farrar's growth estimate, claiming his reliance on the "b x r" result for a two-year period represents a complete departure from the customary staff practice of analyzing at least five years data as a basis for this calculation (App. Ex. 4A, pp. 7-12). Mr. Maugans goes so far as to suggest that Mr. Farrar selected only the numbers he needed to produce an artificially low equity cost (App. Ex. 4A, p. 8). He points out that had Mr. Farrar used the method sponsored by the staff in the company's prior case (Case No. 78-677-EL-AIR), a growth rate of 3.73 percent would result (App. Ex. 4A, pp. 10-11). He also presented an exhibit depicting the growth component which would be produced by applying the method described in the staff reports issued in twelve other electric rate proceedings to Illuminating Company data (App. Ex. 4L). These fall generally in the area of 3.5 percent. The Commission believes that Mr. Maugans' criticisms are unwarranted, that his insinuations are improper, and that his comparisons are largely irrelevant.

It must be remembered that the "growth" element of the DCF formula is actually "expected growth" and, as such, is not susceptible to empirical measurement (S.R. p. 28; Tr. XXIV, p. 26). Thus, a witness must rely on judgment in making this growth determination, and different

witnesses may have legitimate differences of opinion as to what constitutes the best evidence upon which to base that judgment. Moreover, the same witness may quite properly reach a different conclusion as to what evidence represents the most reliable guide to future growth prospects in two different cases, based on the facts of each case. The Commission finds nothing untoward in the fact that Mr. Farrar chose to regard different data sets as more pertinent for purposes of his recommendation in these proceedings than those which other staff witnesses have drawn upon for growth estimates in other cases. The Commission readily concedes that the staff has never used less than a five year "b x r" for determining expected growth, although it is also evident from applicant's exhibit that the staff has, in fact, used a variety of different analyses in those cases cited (App. Ex. 4L). Mr. Farrar has fully described the basis for his growth estimate in this case, and his recommendation must stand or fall on its merits. It should not and will not be dismissed merely because it differs from staff conclusions in other cases.

The Commission must begin the review of Mr. Farrar's growth analysis by correcting applicant's repeated misstatement that the staff witness's estimate of growth is based only on a two-year "b x r" calculation (App. Ex. 4A, p. 7; Tr. XXIV, p. 20; App. Brief, p. 37). This is plainly not the fact. Mr. Farrar's analysis begins with his observation that the result of the "b x r" calculation for the year 1978 showed a precipitious drop from the "b x r" for prior years (Tr. XXIV, pp. 24-25). For the years 1978 and 1979, "b x r" was 1.84 percent and 2.48 percent, respectively, yielding an average "b x r" for this two-year period of 2.16 percent (Staff Ex. 11, p. 22). Mr. Farrar compared this figure to the "b x r" computed for the five-year period, 1975 through 1979, of 3.58 percent and the ten-year period, 1970 through 1979, of 3.77 percent (S.R., p. 29). The magnitude of the disparity prompted Mr. Farrar to explore

possible explanations for this break in the historic growth pattern. He noted that earnings per share for 1979 were well below the experience of 1974 (S.R., p. 29). As calculated by Mr. Farrar, the log-linear growth rate of earnings since 1974 was 0.76 percent (S.R., p. 29). For the period since 1975, it was 1.98 percent (S.R., p. 29). This evidence led Mr. Farrar to conclude that there may have been a basic restructuring between the yield and growth components of investor requirements relative to this utility (Staff Ex. 11, p. 9). This interpretation is certainly plausible in light of the decline in applicant's stock prices (Staff Ex. 11, p. 14). Growth expectations appear to have declined, while yield requirements have obviously increased. The use of a five-year average "b x r" would not be consistent with this explanation of the basis for the drastic change in "b x r" between 1977 and 1978. Based on the data discussed above, estimates of earnings growth from other sources (Tr. XXIV, p. 21), and historical earnings growth rates, both compound and log-linear (Tr. XXIV, p. 24), Mr. Farrar's opinion was that 2.25 percent represents a reasonable estimate of investor's future growth expectations.

Both of applicant's witnesses attempted to minimize the significance of earnings growth rates in determining the estimated growth in dividends for purposes of the DCF calculation (App. Ex. 8, p. 23; App. Ex. 4A, p. 11). It should be obvious, however, that a policy of continuing to increase dividends in the absence of corresponding increases in earnings can only be maintained for so long. As witness Maugans contends, applicant's dividend growth has been relatively stable for some time; but we have already seen that earnings growth has not kept pace (S.R., p. 29). This should in no way be taken as a criticism of applicant's dividend policy. It does, however, tend to support Mr. Farrar's position with respect to the import of the abrupt change in "b x r" in 1978. In 1978, applicant's divi-

dend payment ratio reached an all-time high (S.R., p. 32), and it was in 1978 that applicant's market-to-book ratio, on an annual basis, fell below 1.0 for the first time (S.R., p. 37). The Illuminating Company had historically been the strongest of the Ohio electrics in terms of market-to-book, but despite the fact that it had exhibited the most stable growth in dividends, and despite the fact that it was paying the second highest actual dividend of the other Ohio electrics, it entered 1978 with the poorest market-to-book ratio of the six companies (S.R., p. 33). Thus, as Mr. Farrar's analysis would suggest, it is certainly possible that by 1978 applicant's investors had come to recognize that the practice of increasing the current dividend without concomitant earnings support was nothing more than a borrowing from future dividends (Staff Ex. 11, pp. 16-17). The historical dividend growth rate is certainly relevant in estimating future growth. However, earnings growth, and its relationship to dividends growth, is deserving of far more attention than either of applicant's witnesses devoted to it.

Having considered applicant's complaint that the period analyzed by Mr. Farrar for purpose of estimating the growth component of the DCF formula was too short, the Commission must, itself, question whether the period examined by Mr. Jeffries may not have been too long. It can be stated without fear of contradiction that the conditions faced by the electric utility industry today are vastly different from those which obtained prior to 1974. Indeed, Mr. Maugans expressly recognized this fact in limiting the risk permium analysis he described in his original testimony to the most recent five years (App. Ex. 4, p. 34). Upon cross-examination by staff counsel, he also agreed that in light of the changed circumstances it was unrealistic to expect the company to return to the earnings level of the period 1968 through 1977 (Tr. X, p. 38). Mr. Maugans listed a number of the more significant of these changed

conditions: unprecedented, sustained inflation; lower sales growth; increased fuel costs; more governmental and regulatory involvement in all aspects of operation; more consumer activism; increased lead times for the construction of generating facilities and the decrease in quality of earnings resulting from the attendant increase in AFUDC charges; and extremely volatile short and long-term interest rates (App. Ex. 4, pp. 34-35). Although it is readily apparent that these factors increase the risk to the equity investor and, accordingly, create much higher yield requirements, it is hard to understand why they should have any sort of sustaining effect on historical growth expectations.

In light of the foregoing discussion, the Commission is of the opinion that Mr. Farrar's estimate of expected growth is more reasonable than that offered by Mr. Jeffries. The 4.0 percent growth projection fails to adequately consider applicant's recent earnings history and is based on an analysis of a time period which includes years in which conditions were far different from those that may reasonably be anticipated in the future. Even if we were to assume the longer time frame to be appropriate, a mere change in the reference from 1968 through 1978, to 1970 through 1979, would produce a significant change in the earnings growth rate. Using the log-linear method, it drops from the 3.2 percent calculated by Mr. Jeffries to approximately 2.5 percent (Tr. XXIV, p. 24). The compound growth rate for the last ten years is just over 2.0 percent (Tr. XXIV, p. 24). Mr. Farrar's recommendation is internally consistent, for he couples his finding of investors' diminished future growth expectations with a recognition of their increased yield requirements. In fact, his recommended cost of equity is, to our knowledge, the highest ever sponsored by a staff witness and, at its upper bound, is certainly well above any heretofore authorized by the Commission. Further, the reasonableness of his 2.25 per-

cent growth rate is confirmed by the results of the risk premium analysis he performed which demonstrates that the use of a higher growth rate would have resulted in a risk differential far in excess of the average for the last five years (S.R., pp. 29-30). Applicant's objections relative to this area should be overruled.

The Commission's acceptance of a 2.25 percent growth component for the DCF calculation does not bring our rate of return inquiry to an end, as each of the witnesses significantly revised his original cost of equity recommendation at hearing. Mr. Jeffries summarized the changes in economic conditions which have occurred since the time his original testimony was filed (App. Ex. 8A, pp. 1-4). Among the most significant of these changes was the Federal Reserve Board's pronouncement of October 6, 1979, with respect to the adoption of a restrictive monetary policy designed to slow inflation. Indeed, the Commission has discussed the impact of this action in several recent rate orders. (See, *e.g.*, *Cincinnati Gas and Electric Company*, Case No. 79-11-EL-AIR [January 7, 1980]; *Toledo Edison Company*, Case No. 79-143-EL-AIR [February 29, 1980]). As Mr. Jeffries observes, the prime rate was in the area of 13 percent in September of 1979. At the outset of the hearing in these matters it was in excess of 19 percent (App. Ex. 8A, p. 3). Mr. Maugans, in explaining the sensitivity of utility stock prices to prevailing interest rates, points out that on October 3, 1979, the price per share of applicant's common stock was $17.625, but by March 5, 1980, it had dropped to $14.25 (App. Ex. 4A, p. 4). Inflation has continued unabated (App. Ex. 8A, p. 3).

There is no doubt that the cost of equity capital to the company increased significantly during the period between October of 1979 and the time these matters came on for hearing at the beginning of April, 1980. The question is, however, how to appropriately recognize these

changes in the cost of capital analysis. It will be recalled that in their original testimony both Mr. Jeffries and Mr. Farrar based their determination of the DCF yield component on the average stock price for a twelve-month period. Both cautioned against the use of spot yields in the calculation. Consistent with that methodology, each of the witnesses updated their yield computations to include more recent market data. Mr. Jeffries used the average price for the twelve months ending with February, 1980 (App. Ex. 8A, p. 4). Mr. Farrar brought his calculation forward through March, 1980, which produced an even higher yield determination; specifically, 11.86 percent (Tr. XXIV, pp. 3-4). This update pushed Mr. Jeffries' original equity return recommendation to the 16.0 to 17.0 percent range (App. Ex. 8A, p. 4). Mr. Farrar's recommendation is now 14.56 to 15.52 percent. Yet despite the fact that Mr. Farrar used precisely the same method as its own witness, applicant now complains that staff's yield determination is unreasonable (App. Ex. 4A, pp. 6-7; App. Brief, p. 38).

Applicant argues that if the return authorized is to reflect current investor requirements, the yield component should be calculated with reference to the average stock price over the last quarter of 1979 and the first quarter of 1980 (App. Ex. 8A, p. 5). As precedent for such a measure, the company cites this Commission's decision in the *Cincinnati Gas and Electric Company* case, *supra*, wherein we did employ a three-month rather than a twelve-month period for determining price based on reasoning similar to that now espoused by the applicant. However, there are factors present here which persuade the Commission that the twelve-month period remains appropriate for purposes of these proceedings.

As indicated above, the period following the Federal Reserve Board's October, 1979, announcement saw a steady rise in the prime rate. In light of additional mone-

tary and credit actions taken by the Board in March of 1980 (App. Ex. 8A, p. 1), this trend was reinforced. At that time, no one could reasonably anticipate that this situation would reverse itself in the near-term, at least not to the degree that has actually been the case (Tr. X, p. 124). On April 21, 1980, the prime rate was 19¾ percent (Tr. X, p. 121), but by May 13, 1980, it had dropped to 16½ percent (Tr. XXVI, p. 73). Since the conclusion of the hearings in these matters, it has fallen to 12 percent (*Wall Street Journal*, June 13, 1980). As Mr. Maugans testified, the utility stock prices should tend to respond to a drop in interest rates somewhat more quickly than the market as a whole (Tr. X, p. 119). This prediction has proved accurate, as applicant's stock has rebounded from an all-time low to where it is now selling in the $17 to $18 per share range.

In light of these developments, Consumers' Counsel argues that the Commission should ignore, as extraordinary, the conditions which prompted the witnesses to revise their cost of equity recommendations (O.C.C. Brief, p. 11). The City of Cleveland advances a similar claim (City of Cleveland Brief, p. 8). Thus, on the one hand, we have the company contending that the data before October of 1979 is irrelevant, while on the other, we are confronted with intervenors' arguments that events since that time should not be considered. All this goes to point up the wisdom of Mr. Farrar's use of a twelve-month period for measuring yield in order to even out short-term fluctuations (Staff Ex. 11, p. 14). Under the circumstances of this case, the Commission believes Mr. Farrar's recommendation to be reasonable, and we accept his determination of the yield component as providing an appropriate basis for the DCF analysis.

Combining Mr. Farrar's yield of 11.86 percent with his estimate of expected growth of 2.25 percent produces a base line cost of equity 14.11 percent. After application

of the appropriate adjustment factors (S.R., p. 29), a range of 14.56 to 15.52 percent results. Although these limits have an aura of precision about them, it is clear from the foregoing discussion that the recommended range is no more than the summation of individual judgments. Given this fact, the Commission concludes that 15.0 percent, which falls at the approximate mid-point of this range, represents a reasonable estimate of the cost of equity capital to this utility.

**Attrition Adjustment:**

Applicant proposes an adjustment of some $13.8 million to account for inflation and to offset earnings erosion subsequent to the test period (App. Ex. 1, Sched. C-3.20, p. 103). The staff opposes the adjustment (S.R., pp. 17-18). Although presented as an expense adjustment, the Commission believes it appropriate to consider this item in connection with our rate of return discussion.

The Commission has had occasion to consider the question of an allowance for attrition in a number of its recent rate decisions. The specific proposals have taken a variety of forms ranging from an augmentation of the rate of return as presented by this company in its last rate case (*Cleveland Electric Illuminating Company*, Case No. 78-677-EL-AIR [May 2, 1979]), to adjustments to cost of service to reflect projected future expenses (See, *e.g.*, *Dayton Power and Light Company*, Case No. 78-92-EL-AIR [March 9, 1979]). The Commission has generally rejected adjustments of this type, finding them to be inconsistent with the test-year concept of rate regulation (*Columbia Gas of Ohio, Inc.* [*Columbus*], Case No. 76-704-GA-AIR [June 29, 1977], aff'd *sub nom Franklin County Welfare Rights Organization v. Public Utilities Commission*, 55 Ohio St. 2d 1 [1978]). Although recognizing that regulated utilities are among the primary victims of inflation due to their inability to readily adjust prices, the Com-

mission has pointed out that reduced regulatory lag and appropriate expense annualizations have served to lessen its impact. More important, perhaps, from the standpoint of regulatory theory, is the fact that investors capitalize the risks of inflation in making their investment decisions. Thus, this element is reflected in the market price of the stock which, in turn, is built into the DCF analysis of the cost of equity upon which the authorized rate of return is based. The Supreme Court has recognized these considerations in upholding Commission decisions denying attrition allowances (*Franklin County Welfare Rights Organization v. Public Utilities Commission, supra; Masury Water Company v. Public Utilities Commission,* 58 Ohio St. 2d 1 [1979]).

Applicant correctly points out that the Commission has, in one prior instance, adjusted the allowed rate of return to recognize the impact of attrition on the resulting revenues (*Columbus and Southern Ohio Electric Company,* Case No. 78-1438-EL-AIR [December 29, 1979]). However, as the Commission was careful to explain in the order cited by applicant, that case involved a company facing a unique combination of circumstances which threatened its basic financial integrity. We do not believe that all those same factors have coalesced in this case. The Commission, therefore, rejects applicant's proposed attrition allowance for those reasons repeatedly stated in prior orders wherein we have considered this subject.

**Rate of Return Summary:**

Applying a cost of equity of 15.0 percent to the equity component of the capital structure approved herein produces, when combined with the findings relative to long-term debt and preferred stock, a weighted cost of capital of 10.82 percent. The Commission is of the opinion that a rate of return of 10.82 is sufficient to provide the company reasonable compensation for the electric service it renders customers affected by these proceedings.

## AUTHORIZED INCREASE

A rate of return of 10.82 percent applied to the jurisdictional rate base of $1,485,734,000 approved for purposes of these proceedings results in an allowable return of $160,756,000. Certain expenses must be adjusted if the gross revenues authorized are to produce this dollar return. These adjustments, which have been calculated in a manner consistent with the findings herein, result in an increase in the allowance for federal income tax of $30,705,000, in the allowance for other taxes of $2,748,000, and in the provision for uncollectibles of $143,000. The net effect of these adjustments is to increase allowable expenses to $682,274,000. Adding the approved dollar return to the allowable expenses results in a finding that applicant is entitled to place rates in effect which will generate $843,030,000 in gross annual operating revenue. This represents an increase of $69,641,000 over the revenues which would be realized under applicant's present rate schedules. Similar calculations for the application area and the City of Cleveland would indicate that increases in gross annual revenues of $47,446,000 and $22,195,000 would be required if the applicant is to realize the dollar return resulting from the application of the authorized rate of return to the respective rate bases. Although our analysis suggests that the existing revenue deficiency is slightly greater in the City of Cleveland than in the application area, applicant has proposed a uniform increase in both rate areas. The Commission is of the opinion that the rates of return on the respective rate bases which result from maintaining uniform rates fall within acceptable limits around the jurisdictional rate of return and that rates may properly be established on a total jurisdiction basis.

Through filed objections to the staff report, several parties have taken exceptions to the staff's failure to address the question of whether the increase proposed by the company complies with guidelines promulgated by the Council

on Wage and Price Stability. The Commission has noted on a number of previous occasions that this agency is charged by statute to decide rate applications in accordance with state law and that the voluntary guidelines cannot limit the level of relief authorized (See, *e.g.*, *Dayton Power and Light Company*, Case No. 78-92-EL-AIR [March 9, 1979]; *Dayton Power and Light Company*, Case No. 79-372-GA-AIR [May 7, 1980]). By its filing in these dockets of March 28, 1980, applicant presented an assessment of its compliance with the guidelines in which it indicates that even a grant of the full relief requested would not exceed the limitations. No other party presented evidence on the subject. The foregoing satisfies the Commission's reporting function.

The Commission is well aware of the fact that this company received rate relief a little over a year ago and that even as hearings were beginning in this case it filed notice of its intention to seek yet another rate increase. Inflation, of course, is the principal cause of applicant's ongoing financial dilemma, particularly with respect to its impact on costs associated with the company's construction program. Neither the company nor the Commission can control inflation, but, as discussed previously, there is reason to hope that the announced cancellation of four generating units will have some positive effects on applicant's financial outlook. There is, however, another area where even a modest improvement could have a significant impact with respect to the company's battle against earnings erosion.

The results of actual operations may be significantly influenced when some of a company's largest generating units exhibit poor equivalent availability. These are the very units which when operating at more reasonable capacity levels, produce the least expensive energy. Davis-Besse is obviously applicant's chief offender, a circumstance the Commission has recognized through the normal-

izing adjustment approved in the cost of service analysis in this case. However, there may be cost-effective improvements which could be pursued with respect to other of applicant's units as well. In its orders in *Columbus and Southern Ohio Electric Company,* Case No. 78-1438-EL-AIR (December 12, 1979) and *Cincinnati Gas and Electric Company,* Case No. 79-11-EL-AIR (January 7, 1980), the Commission described a staff program, undertaken in connection with the Department of Energy, to investigate the costs and benefits associated with improved power plant productivity. Staff witness Hunt offered testimony in these proceedings commending applicant for the steps taken to date to improve unit availability and urging that these efforts be continued (Staff Ex. 9, pp. 9-10). The staff recommends that the company be required to submit quarterly reports on the immediate past performance of its generating units, in a form to be agreed upon by the applicant and the staff, to be used in establishing a statewide power plant productivity data base to assist in monitoring power plant performance (Staff Ex. 9, pp. 10-11). In recognition of the importance the Commission attaches to this subject, we will so order.

## TARIFFS

The recommendations offered by the staff after its review of applicant's proposed tariffs drew relatively few objections (S.R., pp. 52-61). Those staff recommendations not subject to specific objection or modification should be implemented. There are, however, several remaining tariff questions which the Commission must consider.

### Customer Charge:

In applicant's last rate case, the Commission adopted a staff recommendation which introduced a customer charge component into applicant's residential and small commer-

cial rate schedules for the first time. This measure was consistent with all other recent electric rate orders. The purpose of the flat charge is to recognize that there are costs incurred by the company merely by virtue of the fact that a customer is on the system, without regard to usage considerations. Applicant's proposed residential tariffs include a customer charge of $3.00, a slight reduction from the $3.05 charge approved in the prior case. The staff considers the charge to be acceptable in light of the customer charges currently in effect for other utilities in the state (Staff Ex. 10, p. 3). Applicant's witness Bingham, who sponsored applicant's proposed tariffs, agreed with staff witness Groves that the concept of a customer charge was theoretically correct (App. Ex. 7A, p. 5). However, he noted that there had been poor customer acceptance of the charge as evidenced by the many complaints received by the company with respect thereto (App. Ex. 7A, p. 5). Customer acceptance is, of course, an important consideration in rate design, but it must be balanced against the also important principle that rates should reflect cost. Given the modest nature of the customer charge proposed and the fact that it actually represents a decrease from that currently in effect, the Commission believes this feature should be retained. It is hoped that customer opposition will diminish as experience is gained with the charge.

**Energy Conservation Rate:**

Applicant's proposed residential tariff continues the energy conservation schedule approved by the Commission in the company's prior rate case. This schedule is available to customers whose dwelling units meet certain insulation and other energy conservation standards. Intervenor City of Cleveland challenged this rate on the basis that it is not cost-justified, a fact which is somewhat ironic in that the Cleveland ordinance from which the complaint and appeal is taken also contains this rate provision. Based on

his analysis of a single study, City of Cleveland witness Rothey concluded that the rate was not cost-based (City of Cleveland Ex. 9, pp. 15-17). Cross-examination indicated that there was other relevant data which might have been considered (Tr. XXV, pp. 50-55), and the witness agreed that there were other considerations to be taken into account in rate designs in addition to cost of service principles (Tr. XXV, p. 49). No further discussion is required as the Supreme Court in *City of Cleveland v. Public Utilities Commission*, S. Ct. Case No. 79-1158 (July 9, 1978), 63 Ohio St. 2d (1980) reviewed this same schedule and determined that it furthered a proper objective. Intervenor's objection is overruled.

**Space Heating and Water Heating Schedules:**

Applicant's tariffs offer a separate rate for space heating and water heating customers whose appliances were installed prior to Commission orders closing the rate in *Cleveland Electric Illuminating Company*, Case No. 71-634-Y (November 28, 1979), Order on Remand (July 3, 1975). In reviewing the history of these provisions, the staff found that the original order closing the rate indicated that "customers" were to be grandfathered, while the language of applicant's tariffs limits the rate to "installations." The staff recommended that this language be amended to conform to the aforementioned orders. Applicant acknowledges that the orders in question do refer to "customers", but points out that the tariffs have always contained the "installation" phraseology. As these tariffs have been accepted for filing by a succession of Commission entries, Applicant argues that the Commission has approved the concept. We need not discuss the implications of these prior entries, for, no matter what they may have said, we now find that the availability of rate should be limited to existing customers. The idea advanced by applicant that some sort of property right attaches to the availability of this

rate is absurd (Tr. XVIII, pp. 28-29). There is no transferable property right in any utility rate. Although grandfathering may, on occasion, be appropriate for existing customers to give effect to equitable considerations, the very idea in closing a rate is that it will eventually disappear through attrition. How will this process proceed at any meaningful pace if the limiting provisions apply to installations rather than customers? Applicant's objection to the staff recommendation is overruled.

**General Commercial Schedule:**

Two questions exists with respect to the company's proposed general service schedule. Applicant proposed to reinstitute a two-part declining block rate in the summer rates contained in this schedule. The staff, although originally recommending rejection of the change, has now dropped its opposition. Applicant's witness Bingham amply supported the return to the two-block rate through his supplemental testimony (App. Ex. 7A, p. 4). This rate design is hereby approved for this schedule.

The second issue which has arisen with respect to this schedule is whether the return being earned from this service is inadequate when compared to the return on other services. Based on the cost of service study submitted in this case (App. Ex. 9, p. 1), applicant concluded that this was, in fact, the case. The staff concurs in this judgment (S.R., pp. 57-58). The Commission, therefore, directs that the proposed distribution of revenue requirements embodied in the rate schedules as originally filed be adjusted so that revenues under the general service schedule more nearly approximate the average return under the other schedules. In accordance with the recommendation of Mr. Bingham, the extent to which this change results in a lower revenue requirements from other customer classes should be recognized through a pro

rata reduction based on existing revenue levels (Tr. XVIII, pp. 27-28).

**Effective Date:**

The general practice of this Commission has been to fix the effective date of tariffs filed pursuant to its rate orders as thirty days following the issuance of the entry accepting the tariffs for filing. The purpose of this delay is to afford affected customers notice of the increase authorized through mailings by the company prior to the date the new rates become applicable. The Commission continues to believe this to be a reasonable practice, but finds circumstances present in this case which compel a departure from this policy.

Section 4909.42 Revised Code provides that if the Commission has not acted upon a rate increase application within 275 days of the date of filing, the applicant utility, upon the filing of an undertaking, may place its proposed rates into effect subject to the condition that amounts collected under rates charged which are in excess of those ultimately determined reasonable by the Commission must be refunded. The Commission makes every effort to issue its rate orders in advance of the expiration of 275-day time period in order to avoid the customer confusion which might result should the refund provision be invoked. Due to the extraordinary length of the hearings in these dockets, this was not possible in this instance. However, applicant has made no attempt to place its proposed rates in effect and the Commission believes that basic principles of fairness dictate that the company not be penalized for its forebearance. The Commission, therefore, finds the appropriate course in these proceedings to be to establish the effective date of the tariffs filed pursuant to this order as the date they are approved by Commission entry. The customer notification requirement will,

of course, be retained; said notice to be mailed to affected customers upon approval of its form by the Commission.

**FINDINGS OF FACT:**

From the evidence of record in these proceedings, the Commission now makes the following findings:

1) The value of all of applicant's property used and useful for the rendition of electric service to the customers affected by this application and complaint and appeal determined in accordance with Section 4909.05 and Section 4909.15 Revised Code as of the date certain of June 30, 1979, is not less than $1,485,734,000.

2) The value of the rate base properly allocable to the application area is not less than $1,030,866,000.

3) The value of the rate base properly allocable to the City of Cleveland is not less than $454,868,000.

4) For the twelve month period ending December 31, 1979, the test period in these proceedings, the revenues, expenses, and income available for fixed charges realized by applicant under its present permanent rate schedules were $773,389,000, $648,678,000, and $124,711,000, respectively.

5) The revenues, expenses, and income available for fixed charges realized by applicant in the application area were $542,489,000, $455,507,000, and $86,982,000, respectively.

6) The revenues, expenses, and income available for fixed charges realized by applicant the City of Cleveland under present rates now continued in effect by the ordinance complained of were $230,900,000, $193,171,000, and $37,729,000, respectively.

7) The total net annual compensation of $124,711,000 represents a rate of return of 8.39 percent on the jurisdictional rate base.

8) The net annual compensation of $86,982,000 realized by applicant in the application area represents a rate of return of 8.44 percent on the allocated rate base.

9) The net annual compensation of $37,729,000 realized by applicant in the City of Cleveland represents a rate of return of 8.29 percent on the allocated rate base.

10) Rates of return of 8.39 percent, 8.44 percent, and 8.29 percent are insufficient to provide applicant reasonable compensation for the electric service rendered customers affected by the application and complaint and appeal.

11) A rate of return of 10.82 percent is fair and reasonable under the circumstances presented by these cases and is sufficient to provide applicant just compensation and return on the value of its property used and useful in furnishing the service described in the application and complaint and appeal.

12) A rate of return of 10.82 percent applied to the the jurisdictional rate base of $1,485,734,000 will result in income available for fixed charges in the amount of $160,756,000.

13) The allowable annual expenses of applicant for purposes of these proceedings are $682,274,000.

14) The allowable gross annual revenue to which applicant is entitled for purposes of these proceedings is the sum of the amounts set forth in Findings 12 and 13, or $843,030,000.

15) Applicant's present tariffs should be withdrawn and cancelled and applicant should submit new tariffs consistent in all respects with the discussion and findings set forth above.

16) The tariffs submitted by applicant shall contain base (or non-fuel) rates and charges sufficient to yield gross revenues which will compensate the company for allowable test period operating expenses, exclusive of fuel costs includable in its fuel adjustment clause, and yield a 10.82 percent rate of return on its rate base of $1,485,734,000.

17) The provisions of these tariffs should be substituted for the provisions of Ordinance No. 1673-79 of the City of Cleveland.

18) Applicant shall be required to submit quarterly reports, in a form to be agreed upon by the company and the staff, detailing the immediate past performance of its generating units.

**CONCLUSIONS OF LAW:**

1) The application herein is filed pursuant to, and this Commission has jurisdiction thereof, under the provisions of Sections 4909.17, 4909.18 and 4909.19 Revised Code; further, applicant has complied with the requirements of the aforesaid statutes.

2) The instant complaint and appeal is filed pursuant to, and this Commission has jurisdiction thereof, under the provisions of Section 4909.34 Revised Code; further, applicant has complied with all applicable statutory requirements.

3) A staff investigation has been conducted and a report duly filed and mailed and public hearings have been held herein, the written notice thereof having complied with the requirements of Section 4909.19 Revised Code.

4) The existing rates and charges now being charged and collected by applicant for electric service to customers affected by this application are insufficient to provide the company with adequate net annual compensation and return

on its property used and useful in the rendition of electric service.

5) The rates for electric service contained in Ordinance No. 1673-79 of the City of Cleveland are insufficient to provide applicant adequate net annual compensation and return on its property used and useful in furnishing the service governed by said ordinance.

6) A rate of return of 10.82 percent is fair and reasonable under the circumstances of these cases and is sufficient to provide applicant just compensation and return on its property used and useful in the rendition of electric service to its customers.

7) Applicant should be authorized to cancel and withdraw its presently effective tariffs on file with this Commission and to file new tariffs consistent in all respects with the discussion and findings set forth above.

8) The provisions of these tariffs should be substituted for the provisions of Ordinance No. 1673-79 of the City of Cleveland.

**ORDER:**

It is, therefore,

ORDERED, That the application of Cleveland Electric Illuminating Company for authority to increase its rates and charges for electric service be, and hereby is granted to the extent provided in this Opinion and Order. It is, further,

ORDERED, That the complaint and appeal of Cleveland Electric Illuminating Company from Ordinance No. 1673-79 of the City of Cleveland be, and hereby is sustained and that relief be, and hereby is authorized to the extent provided in this Opinion and Order. It is, further,

ORDERED, That applicant be, and hereby is authorized to cancel and withdraw its present permanent tariffs and to file new tariffs consistent with the discussion and findings set forth above. Upon receipt of three (3) complete copies of tariffs conforming to this Opinion and Order, the Commission will review and approve same by entry. It is, further,

ORDERED, That the effective date of the new tariffs shall be the date said tariffs are accepted for filing. The new rates contained therein shall be applicable to all service rendered on or after the effective date. It is, further,

ORDERED, That applicant shall immediately commence notification of its customers of the increase in rates authorized herein by insert or attachment to its billings, by special mailing, or by a combination of these methods. Applicant shall submit a proposed form of notice to the Commission when it files its tariffs for approval and the Commission will review same and, if proper, approve it by entry. It is, further,

ORDERED, That applicant submit quarterly reports in a form to be agreed upon the company and the staff detailing the immediate past performance of its generating units. It is, further,

ORDERED, That all objections and motions not specifically discussed within this Opinion and Order or rendered moot thereby be, and hereby are overruled and denied. It is, further,

ORDERED, That copies of this Opinion and Order be served upon all parties of record.

THE PUBLIC UTILITIES
COMMISSION OF OHIO

/s/ WILLIAM S. NEWCOMB, JR.
(Chairman)

MICHAEL DELBANE
Voted no.

/s/ STEPHEN A. REILLY

(Commissioners)

Entered in the Journal

July 10, 1980

A True Copy

DAVID M. POLK

David M. Polk
Secretary

# APPENDIX K

## OHIO STATUTES

### OHIO REVISED CODE

**§ 4905.13 System of accounts for public utilities.** (GC § 499-14)

The public utilities commission may establish a system of accounts to be kept by public utilities or railroads, including municipally owned or operated public utilities, or may classify said public utilities or railroads and establish a system of accounts for each class, and may prescribe the manner in which such accounts shall be kept. Such system shall, when practicable, conform to the system prescribed by the department of taxation. The commission may prescribe the forms of accounts, records, and memorandums to be kept by such public utilities or railroads, including the accounts, records, and memorandums of the movement of traffic as well as of the receipts and expenditure of moneys, and any other forms, records, and memorandums which are necessary to carry out Chapters 4901., 4903., 4905., 4907., 4909., 4921., 4923., and 4925. of the Revised Code. The system of accounts established by the commission and the forms of accounts, records, and memorandums prescribed by it shall not be inconsistent, in the case of corporations subject to the act of congress entitled "An act to regulate commerce" approved February 4, 1887, and the acts amendatory thereof and supplementary thereto, with the systems and forms established for such corporations by the interstate commerce commission. This section does not affect the power of the public utilities commission to prescribe forms of accounts, records, and memorandums covering information in addition to that required by the interstate commerce commission. The public utilities commission may, after hearing had upon its own motion or complaint, prescribe by order the accounts

in which particular outlays and receipts shall be entered, charged, or credited. Where the public utilities commission has prescribed the forms of accounts, records, or memorandums to be kept by any public utility or railroad for any of its business, no such public utility or railroad shall keep any accounts, records, or memorandums for such business other than those so prescribed, or those prescribed by or under the authority of any other state or of the United States, except such accounts, records or memorandums as are explanatory of and supplemental to the accounts, records, or memorandums prescribed by the commission. The commission shall at all times have access to all accounts kept by such public utilities or railroads and may designate any of its officers or employees to inspect and examine any such accounts. The auditor or other chief accounting officer of any such public utility or railroad shall keep such accounts and make the reports provided for in sections 4905.14 and 4907.13 of the Revised Code. Any auditor or chief accounting officer who fails to comply with this section shall be subject to the penalty provided for in division (C) of section 4905.99 of the Revised Code. The attorney general shall enforce such section upon request of the public utilities commission by mandamus or other appropriate proceedings.

HISTORY: GC § 499-14; 103 v 804(812), § 27. Eff 10-1-53. Analogous to former GC § 614-10.

**§ 4905.18 Depreciation account.** (GC § 614-49)

Every public utility shall carry a proper and adequate depreciation or deferred maintenance account, whenever the public utilities commission, after investigation, determines that a depreciation account can be reasonably required. The commission shall ascertain, determine, and prescribe what are proper and adequate charges for depreciation of the several classes of property for each public utility. The public utility commission shall require every

telephone company to carry a proper and adequate depreciation or deferred maintenance account and shall ascertain, determine, and prescribe what are proper and adequate charges in each exchange area of such company. The charge for depreciation shall be such as will provide the amount required over the cost and expense of maintenance to keep the property of the public utility in a state of efficiency corresponding to the progress of the art or industry. The commission may prescribe such changes in such charges for depreciation as it finds necessary.

HISTORY: GC § 614-49; 102 v 549(563), § 51; 125 v 613(614). Eff 10-26-53.

**§ 4905.20 Abandonment of facilities.**

No railroad as defined in section 4907.02 of the Revised Code, operating any railroad in this state, and no public utility as defined in section 4905.02 of the Revised Code furnishing service or facilities within this state, shall abandon or be required to abandon or withdraw any main track or depot of a railroad, or main pipe line, gas line, telegraph line, telephone toll line, electric light line, water line, sewer line, steam pipe line, or any portion thereof, pumping station, generating plant, power station, sewage treatment plant, or service station of a public utility, or the service rendered thereby, which has once been laid, constructed, opened, and used for public business, nor shall any such facility be closed for traffic or service thereon, therein, or thereover except as provided in section 4905.21 of the Revised Code. Any railroad or public utility violating this section shall forfeit and pay into the state treasury not less than one hundred dollars, nor more than one thousand dollars, and shall be subject to all other legal and equitable remedies for the enforcement of this section and section 4905.21 of the Revised Code.

HISTORY: GC § 504-2; 107 v 525; 108 v Pt I 372; 129 v. 501. Eff 9-19-61.

**§ 4905.22 Service and facilities required; unreasonable charge prohibited.** (GC §§ 614-12, 614-13)

Every public utility shall furnish necessary and adequate service and facilities, and every public utility shall furnish and provide with respect to its business such instrumentalities and facilities, as are adequate and in all respects just and reasonable. All charges made or demanded for any service rendered, or to be rendered, shall be just, reasonable, and not more than the charges allowed by law or by order of the public utilities commission, and no unjust or unreasonable charges shall be made or demanded for, or in connection with, any service, or in excess of that allowed by law or by order of the commission.

HISTORY: GC §§ 614-12, 614-13; 102 v 549(553), § 14; 102 v 549(554), § 15. Eff 10-1-53.

**§ 4909.15 Fixation of reasonable rate.**

(A) The public utilities commission, when fixing and determining just and reasonable rates, fares, tolls, rentals, and charges shall determine:

(1) The valuation as of the date certain of the property of the public utility used and useful in rendering the public utility service for which rates are to be fixed and determined. The valuation so determined shall be the total value as set forth in division (J) of section 4909.05 of the Revised Code, and a reasonable allowance for materials and supplies and cash working capital, as determined by the public utilities commission. The commission may, in its discretion, permit a reasonable allowance for construction work in progress but, in no event, may any allowance for construction work in progress be made by the commission until it has determined, after a physical inspection, that the particular construction project is at least seventy-five percent complete.

(2) A fair and reasonable rate of return to the utility on the valuation as determined in division (A)(1) of this section;

(3) The dollar annual return to which the utility is entitled by applying the fair and reasonable rate of return as determined under division (A)(2) of this section to the valuation of the utility determined under division (A)(1) of this section;

(4) The cost to the utility of rendering the public utility service for the test period less the total of any interest on cash or credit refunds paid, pursuant to section 4909.42 of the Revised Code, by the utility during the test period. Federal, state, and local taxes imposed on or measured by net income may, in the discretion of the commission, be computed by the normalization method of accounting, provided the utility maintains accounting reserves that reflect differences between taxes actually payable and taxes on a normalized basis, provided that no determination as to the treatment in the rate making process of such taxes shall be made that will result in loss of any tax depreciation or other tax benefit to which the utility would otherwise be entitled, and further provided that such tax benefit as redounds to the utility as a result of such a computation may not be retained by the company, used to fund any dividend, or utilized for any purpose other than the defrayal of the operating expenses of the utility and the defrayal of the expenses of the utility in connection with construction work.

(B) The public utilities commission shall compute the gross annual revenues to which the utility is entitled by adding the dollar amount of return under division (A)(3) of this section to the cost of rendering the public utility service for the test period under division (A)(4) of this section.

(C) The test period, unless otherwise ordered by the public utilities commission, shall be the twelve-month

period beginning six months prior to the date the application is filed and ending six months subsequent to that date. The revenues and expenses of the utility shall be determined during the test period. The date certain shall be not later than the date of filing.

(D) When the public utilities commission is of the opinion, after hearing and after making the determinations under divisions (A) and (B) of this section, that any rate, fare, charge, toll, rental, schedule, classification, or service, or any joint rate, fare, charge, toll, rental, schedule, classification, or service rendered, charged, demanded, exacted, or proposed to be rendered, charged, demanded, or exacted, is, or will be, unjust, unreasonable, unjustly discriminatory, unjustly preferential, or in violation of law, that the service is, or will be, inadequate, or that the maximum rates, charges, tolls, or rentals chargeable by any such public utility are insufficient to yield reasonable compensation for the service rendered, and are unjust and unreasonable, the commission shall:

(1) With due regard among other things, to the value of all property of the public utility actually used and useful for the convenience of the public as determined under division (A)(1) of this section, excluding from such value the value of any franchise or right to own, operate, or enjoy the same in excess of the amount, exclusive of any tax or annual charge, actually paid to any political subdivision of the state or county, as the consideration for the grant of such franchise or right, and excluding any value added to such property by reason of a monopoly or merger, with due regard in determining the dollar annual return under division (A)(3) of this section to the necessity of making reservation out of the income for surplus, depreciation, and contingencies, and;

(2) With due regard to all such other matters as are proper, according to the facts in each case,

(a) Including a fair and reasonable rate of return determined by the commission with reference to a cost of

debt equal to the actual embedded cost of debt of such public utility,

(b) But not including the portion of any periodic rental or use payments, representing that cost of property which is included in the valuation report under divisions (F) and (G) of section 4909.05 of the Revised Code, fix and determine the just and reasonable rate, fare, charge, toll, rental, or service to be rendered, charged, demanded, exacted, or collected for the performance or rendition of the service that will provide the public utility the allowable gross annual revenues under division (B) of this section, and order such just and reasonable rate, fare, charge, toll, rental, or service to be substituted for the existing one. After such determination and order no change in the rate, fare, toll, charge, rental, schedule, classification, or service, shall be made, rendered, charged, demanded, exacted, or changed by such utility without the order of the commission, and any other rate, fare, toll, charge, rental, classification, or service is prohibited.

(E) Upon application of any person or any public utility, and after notice to the parties in interest and opportunity to be heard as provided in Chapters 4901., 4903., 4905., 4907., 4909., 4921., and 4923. of the Revised Code for other hearings, has been given, the commission may rescind, alter, or amend an order fixing any rate, fare, toll, charge, rental, classification, or service, or any other order made by the commission. Certified copies of such orders shall be served and take effect as provided for original orders.

In no event shall an allowance for construction work in progress under division (A)(1) of this section exceed twenty percent of the total valuation as stated in such division not including such allowance.

*HISTORY: 137 v H 230 (Eff 10-9-77); 138 v H 657 (Eff 9-24-79); 138 v H 736. Eff 10-16-80.

## OHIO ADMINISTRATIVE CODE

### § 4901:1-9-05 Uniform classification of accounts for electric utilities: FPC, 1961

The system of accounts and records, identified and designated as "Uniform System of Accounts Prescribed for Public Utilities and Licensees, effective January 1, 1961," as adopted by the Federal Power Commission, is adopted by this Commission effective as of January 1, 1961, for electric light companies operating within the State of Ohio which are subject to the jurisdiction of the Federal Power Commission except to the extent that the provisions of said Uniform System of Accounts are inconsistent in any way with the outstanding orders of this Commission pertaining to the accounting treatment to be followed with respect to emergency facilities and the Federal income tax results thereof and with respect to accelerated depreciation and the Federal income tax results thereof. This Commission reserves to itself the right to require the creation and maintenance of such additional accounts as may hereafter be prescribed, to cover the accounting procedure of such electric light companies operating in the State of Ohio. Each such public utility shall carry on its books, in addition to such additional accounts as may hereafter be prescribed by this Commission, the accounts and records prescribed in said Uniform System of Accounts effective January 1, 1961, for a public utility of its class, and shall accordingly keep such accounts in accordance with the requirements, definitions and instructions contained and set forth in said uniform system of accounts except to the extent that the provisions of said Uniform System of Accounts are inconsistent in any way with the outstanding orders of this Commission pertaining to the accounting treatment to be followed with respect to emergency facilities and the Federal income tax results thereof and with respect to accelerated depreciation and

the Federal income tax results thereof in the stead and in lieu of the accounts and records prescribed by the provisions of rule 4901:1-9-02.

HISTORY: Eff. 1-20-63
Former Rule 25.05

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Case No. 82-704

IN THE SUPREME COURT OF THE UNITED STATES
October Term, 1982

THE CLEVELAND ELECTRIC ILLUMINATING COMPANY,
*Appellant,*

vs.

THE PUBLIC UTILITIES COMMISSION OF OHIO,

and

OFFICE OF CONSUMERS' COUNSEL,
*Appellees.*

ON APPEAL FROM THE SUPREME COURT OF OHIO

# MOTION OF APPELLEE, OFFICE OF THE CONSUMERS' COUNSEL, TO DISMISS APPEAL, OR IN THE ALTERNATIVE, MOTION TO AFFIRM

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Ohio Rev. Code §4905.22.....10, 26, 27, 32

## STATEMENT OF THE CASE

Appellee, the Office of the Consumers' Counsel, will confine its statement of the case to those points with which it disagrees with the Appellant's Statement of the Case in Appellant's statement in support of its jurisdiction. The procedural aspects of this case with respect to the course of proceedings below, as set forth in Appellant's Jurisdictional Statement, are correct except as noted hereafter.

As Exhibit I attached to Appellant's Jurisdictional Statement reveals, the procedural history of the issue on which the instant appeal is based is complicated. It bears emphasizing that the proceeding herein appealed from is nothing more than the mechanical manifestation of the Public Utilities Commission of Ohio's compliance with the Mandate issued to it by the Ohio Supreme Court in Consumers' Counsel v. Pub.

Util. Comm., 67 Ohio St.2d 153, 423 N.E.2d 820 (1981), already reviewed by this Court in The Cleveland Electric Illuminating Company v. Office of Consumers' Counsel, et al., United States Supreme Court Case No. 81-1002 (February 25, 1982); 71 L.Ed.2d 455 (1982).

Appellant raises no new issues in this appeal, but rather seeks merely to relitigate the decision of the Ohio Supreme Court in Consumers' Counsel v. Pub. Util. Comm., supra. The question faced by the Ohio Court was simply whether costs associated with terminated nuclear units were a proper cost of service upon which a utility's rates could be based. At question was Ohio Rev. Code §4909.15(A)(4), which statute governs ratemaking in Ohio. The crux of the controversy in this case is best stated in the words of the Ohio Supreme Court:

> The controversy surrounding the cancelled nuclear power plants focuses

primarily on R.C. 4909.15(A)(4), which delineates the service-related costs that a utility may recover from its ratepayers. This section states in relevant part:

"The public utilities commission, when fixing and determining just and reasonable rates, fares, tolls, rentals, and charges shall determine:

"***

"(4) The cost to the utility of rendering the public utility service for the test period***."

The commission urges that "an expenditure by a utility can be considered a cost of rendering the public utility service if it fails in fact to achieve its intended purpose*** [if] the expense was reasonably calculated to provide [future] utility service at a reasonable cost." The underpinnings for the commission rationale may be found in those statutory provisions that require utilities to maintain adequate service presently and for the foreseeable future. See, e.g., R.C. 4905.22 (adequate service and facilities).

Notwithstanding the provisions that impose a duty on utility companies to plan for the future, the question under R.C. 4909.15(A)(4) remains whether the cancelled plant expenditures represent "[t]he cost to the utility of rendering the public utility service for the test period." Test period considerations aside, what the company sought and what the commission granted was the amorti-

zation as service-related costs of an investment that never provided any service whatsoever to the utility's customers.

We seriously question whether the General Assembly contemplated that the commission would treat the type of expenditures controverted herein as costs under R.C. 4909.15(A)(4). The now terminated nuclear plants represented a major capital investment that ultimately would have been included in the rate base under R.C. 4909.15(A)(1), had the projects not been cancelled. It is our opinion that R.C. 4909.15(A)(4) is designed to take into account the normal, recurring expenses incurred by utilities in the course of rendering service to the public for the test period.[8] A nonexhaustive list of such expenses would include reasonable expenditures for repairs, maintenance, personnel-related costs, administrative expenses, and taxes.

The extraordinary loss sustained by CEI in connection with the terminated nuclear plants cannot be transformed into an ordinary operating expense pursuant to R.C. 4909.15(A)(4) by commission fiat. The commission's statement that "[c]ancellation does not create a past loss, but gives rise to a current cost" is unpersuasive. Under this rationale we question whether there could ever be a "past loss" the return of which would not be recoverable in future ratemaking proceedings notwithstanding the commission's assertion to the contrary. The commission's characterization of the investment in the

> four terminated plants as "cost" under R.C. 4909.15(A)(4) in light of what we perceive to be the legislative intention underlying that section is unreasonable. Therefore, to the extent that the commission's order in regard to the cancelled plants is predicated on R.C. 4909.15(A)(4), the order cannot stand.
>
> Consumers' Counsel v. Pub. Util. Comm., 67 Ohio St.2d 153, 423 N.E.2d 820 (1981).

This excerpt from the court's opinion clearly demonstrates the limited scope of the issue on appeal. As noted by Appellant, this Court dismissed the appeal from the Ohio Supreme Court decision above in Case No. 81-1002 (February 25, 1982).

Appellant correctly claims that Appellee argued to this Court in Case No. 81-1002 that a constitutional question was not timely raised nor ruled upon by the Ohio Supreme Court. However, Appellant is mistaken in its insinuation that, only after this Court dismissed its appeal in Case No. 81-1002, did Appellee then intervene in Appellant's subsequent appeal to the Ohio Su-

preme Court from Public Utilities Commission of Ohio Case No. 81-1096-EL-COI (COI Order) and argue that the Ohio Court had, indeed, decided the constitutional question. The accurate facts are that Appellee did intervene in Appellant's appeal from the COI Order in a timely fashion pursuant to Ohio Supreme Court rules. Appellee argued, not that the Ohio Court had decided the constitutional question, but rather that Appellant's attempt to litigate an already litigated issue with identical facts on new grounds was barred by the doctrine of res judicata, as discussed below.

Additionally, Appellant continues to assert its timeliness in raising a constitutional question in spite of this Court's dismissal of Case No. 81-1002 for want of a properly presented federal question. The Cleveland Electric Illuminating Company v. Office of the Consumers' Counsel, et al.

supra (February 25, 1982). The plain fact is that there is no constitutional question here; the Ohio Supreme Court has clearly limited its decision to a determination as to what costs appropriately fall within the meaning of Ohio Rev. Code §4909.15(A)(4). There is nothing inherently unconstitutional in excluding from the cost of service the costs of cancelled generating plants which will never provide service.

Thus, this Court, faced now with the same appeal faced by it less than a year ago should, once again, dismiss it on the bases set forth below.

## MOTION TO DISMISS AND IN THE ALTERNATIVE, MOTION TO AFFIRM

Pursuant to Supreme Court Rule 16.1(b), and 16.1(d) Appellee, Office of the Consumers' Counsel, hereby moves that this Court dismiss the Appeal of the Cleveland Electric Illuminating Company as improperly ta-

ken from the Supreme Court of Ohio under 28 U.S.C. §1257(2). In the alternative, the Office of the Consumers' Counsel moves that this Court affirm the decision of the Supreme Court of Ohio rendered in the case below.

## ARGUMENT IN SUPPORT OF MOTION TO DISMISS

The Appellant has invoked the jurisdiction of this Court under 28 U.S.C. §1257 (2), which states in pertinent part:

> Final judgments or decrees rendered by the highest court of a state in which a decision could be had, may be reviewed by the Supreme Court as follows:
>
> * * * *
>
> (2) By appeal, where is drawn in question the validity of a statute of any state on the ground of its being repugnant to the Constitution treaties or laws of the United States, and the decision is in favor of its validity.
>
> * * * *

The express language of 28 U.S.C. §1257(2) requires that the highest court of

a state render a decision favoring the validity of a state statute before review of the state court decision may be sought in the Supreme Court of the United States. The necessary predicate of an appeal under 28 U.S.C. §1257(2) is, therefore, that the validity of the state statute in question must first be challenged in the state court. Where the highest court of a state is not called upon to review a statute claimed to be in conflict with the United States Constitution, or where that state court renders a decision which does not address the validity of the statute, an appeal under 28 U.S.C.A. §1257(2) will not lie. Kulko v. Superior Court of California, 436 U.S. 84 (1978).

In the present case the Appellant is again trying to present arguments already considered by this Court regarding its claim that it properly raised the issue of

the constitutional validity of Ohio Revised Code §§4905.22 and 4909.15(A)(4).

This Court on February 25, 1982 dismissed Appellant's appeal from Consumers' Counsel v. Pub. Util. Comm., 67 Ohio St.2d 153, 423 N.E.2d 820 (1981), "for want of a properly presented federal question". The Cleveland Electric Illuminating Company v. Office of Consumers' Counsel, et al., United States Supreme Court Case No. 81-1002 (February 25, 1982), 71 L. Ed.2d 455 (1982). CEI now wishes to try to invoke this Court's jurisdiction through this back door request seeking review of the same issue presented in Consumers' Counsel, supra.

The appeal in the instant case is brought from the Ohio Public Utilities Commission's response (PUCO Case No. 81-1096-EL-COI, decided October 21, 1981) to the Ohio Supreme Court's remand in Consumers' Counsel v. Pub. Util. Comm., 67 Ohio St.2d

153, 423 N.E.2d 820 (1981). This appeal is simply a relitigation of the same questions contained in Appellant's previous jurisdictional statement, which the Court addressed by summary dismissal.

Appellant presents herein the same questions presented to this Court in its prior statement of jurisdiction. The questions set forth in the Jurisdictional Statement in the former appeal are as follows:

QUESTIONS PRESENTED

1. May the State of Ohio, by statute, constitutionally require a public utility to invest its capital to provide adequate service for the convenience of the public in the future and simultaneously prohibit, by statute, the utility from recovering through rates such capital when prudently invested?

2. May the State of Ohio, by statute, constitutionally prohibit a public utility from recovering through rates its capital, prudently invested for the convenience of the public where the undisputed facts show that the utility, and its investors, have never been compensated through the authorized or

achieved rate of return for the risk of exclusion of such costs from rates?

The Cleveland Electric Utility Company v. Office of Consumers' Counsel, et al., United States Supreme Court Case No. 81-1002 (February 25, 1982); 71 L. Ed.2d 455 (1982).

* * * *

In the case sub judice, Appellant presents the following questions in its Jurisdictional Statement:

QUESTIONS PRESENTED

1. May the State of Ohio, by statute constitutionally require a public utility to invest its capital for the convenience of the public to provide adequate service in the future and simultaneously prohibit, by statute, that utility from recovering through rates such capital when prudently invested?

2. May the State of Ohio, by statute constitutionally prohibit a public utility from recovering through rates its capital, prudently invested for the convenience of the public, where the undisputed facts show that the utility, and its investors, have never been compensated through the authorized rate of return for the risk of exclusion of such costs from rates?

The Cleveland Electric Illuminating Company vs. the Public Utilities Com-

mission of Ohio, et al., United States Supreme Court Case No. 82-704.

Clearly Appellant currently seeks review of the same questions already considered by this Court in Case No. 81-1002.

It bears repeating that this appeal is brought from a proceeding which, although captioned independently, cannot be separated from the Ohio Court's decision in Consumers' Counsel, supra. The COI Order was merely a continuation of the earlier proceedings requiring compliance with the Ohio Court's Mandate. Practically speaking, Appellant requests that this Court, having already denied review of the Ohio Court's decision, less than a year ago, step into the proceeding at a different, later time to gain results already denied to Appellant. It follows that, if Appellant failed to raise properly any federal question in Consumers' Counsel, supra, it cannot cure that failure by an attempt to raise a fed-

eral question when the Public Utilities Commission of Ohio merely complies with the Mandate of the Ohio Supreme Court in Consumers' Counsel.

Rule 15.1(a) of the Rules of the Supreme Court of the United States (U.S. Sup. Ct. Rule 15, 28 U.S.C.A.) requires that a jurisdictional statement contain the questions to be presented by the appeal. Many decisions have labelled a Jurisdictional Statement as the indicator of what issues the Supreme Court has decided in a summary disposition. Mercado v. Rockefeller, 502 F.2d 666 (2d Cir. 1974); Cert. den. 420 U.S. 925 (1975). The Office of Consumers' Counsel submits that this Court has already disposed of the questions submitted in this appeal by its dismissal in Case No. 81-1002.

Furthermore, this Court has ruled on numerous occasions that summary affirmances and dismissals without doubt reject the

specific challenges presented in the Statement of Jurisdiction. Mandel v. Bradley, 432 U.S. 173 (1977). This Court, in its Per Curiam opinion of the constitutionality of Maryland's Election Code, emphasized that summary actions should not be understood as breaking new ground, but as applying principles established by prior decisions to the particular facts involved. This Court further indicated that summary affirmances and dismissals prevent lower courts from coming to opposite conclusions on the precise issues presented and necessarily decided by the issues in the cases summarily dismissed. Mandel v. Bradley, supra.

Since the questions presented are identical in the two CEI appeals, it should follow, pursuant to Mandel, supra, that the prior decision is dispositive of the issues presented in this appeal.

Moreover, it is equally clear that a summary disposition either by affirmance or by dismissal is a disposition on the merits and should not need to be reconsidered by the Court. Hicks v. Miranda, 422 U.S. 332 (1975). Appellant has had its day in Court, and has been unsuccessful. Appellant, having failed to obtain this Court's review of a claimed federal question in its appeal from Consumers' Counsel, cannot revive its already unsuccessful arguments in an appeal from an order which simply carried out the Ohio Court's Mandate. The summary dismissal of the issues presented in Case No. 81-1002 is, therefore, dispositive of the issues presented herein.

It is also clear that relitigation of the identical facts on grounds either previously presented or grounds Appellant failed to present in a proper and timely

fashion is barred by the doctrine of res judicata.

The doctrine of res judicata operates to bar repetitious suits involving the same cause of action. The doctrine is based upon considerations of economy of judicial time and public policy favoring the establishment of certainty in legal relations. Sea-Land Service v. Gaudet, 414 U.S. 573, 578-579 (1974). This Court has also previously noted that res judicata is founded upon "the generally recognized public policy that there must be some end to litigation and that when one appears in Court to present his case, is fully heard, and the constituted issue is decided against him, he may not later renew the litigation in another Court." Heiser v. Woodruff, 327 U.S. 726, 733 (1946).

The Ohio Supreme Court in Consumers' Counsel v. Pub. Util. Comm., 67 Ohio St.2d

153, 423 N.E.2d 820 (1981) disallowed recovery, as an allowable operating expense, of the costs associated with the cancelled plants. This Appellant in Case No. 81-1002 sought review by this Court of the decision of the Ohio Supreme Court in Consumers' Counsel, supra. The Court dismissed Appellant's appeal in Case No. 81-1002 for failure to properly present a federal question.

In accordance with the Opinion of the Ohio Supreme Court in Consumers' Counsel, supra, the Public Utilities Commission of Ohio reduced Appellant's rates, removing therefrom the expenditures associated with the terminated nuclear units. Appellant prosecuted an appeal to the Ohio Supreme Court from the decision of the Public Utilities Commission of Ohio implementing the mandate of the Ohio Supreme Court in Consumers' Counsel, supra, arguing that the Court's original determination in Consum-

ers' Counsel was incorrect. Following the filing of a motion to dismiss by the Office of the Consumers' Counsel responding to said appeal, the Ohio Supreme Court dismissed Appellant's appeal.

Appellant in the instant proceeding was an intervening Appellee in Consumers' Counsel and did present numerous arguments in favor of the validity of the Public Utilities Commission's decision in Case No. 79-537-EL-AIR before the Ohio Supreme Court. Subsequently, Appellant sought to present perceived constitutional issues to this Court for the first time in Case No. 81-1002, never before presented to the Public Utilities Commission and presented to the Ohio Court only after its decision in Consumers' Counsel.

It is apparent that Appellant had the opportunity to present its constitutional arguments, as an intervening Appellee, both

to the Public Utilities Commission of Ohio and the Ohio Court, in Consumers' Counsel, supra. Appellant is now, through this second proceeding, seeking to present an argument which was not made in a timely manner in Consumers' Counsel, supra.

This Court was faced with a similar situation in Grubb v. Pub. Util. Comm., 281 U.S. 470 (1930). In Grubb this Court stated:

> In his bill the appellant assails the validity of the order upon one ground not brought to the attention of the state court - a ground arising out of the granting to another interstate motor line of a certificate to operate busses over a route including the loop at Portsmouth; and he insists that this ground of objection is not concluded by the judgment of the state court, and therefore is open to examination and adjudication upon its merits by the district court. But the judgment has a broader operation as res judicata than is thus suggested. The certificate referred to was granted several months before the appellant applied for a certificate and he had personal knowledge of it from the time it was granted. It was shown upon the records of the commission and was easily accessible when the hearing was had upon his applica-

tion. Thus it is a matter which, if having the bearing now suggested, could have been brought to the attention of the commission either at that hearing or in his request for a rehearing (543, General Statutes); and, if it was not then given proper effect, he could have brought it to the attention of the state court and have made the same claim in respect of it that is now made in his bill.

The thing presented for adjudication in the case in the state court was the validity of the order, and it was incumbent of the appellant to present in support of his asserted right of attack every available ground of which he had knowledge. He was not at liberty to prosecute that right by piecemeal, as by presenting a part only of the available grounds and reserving others for another suit, if failing in that.

As the ground just described was available but not put forward, the appellant must abide the rule that a judgment upon the merits in one suit is res judicata in another where the parties and subject-matter are the same, not only as respects matters actually presented to sustain or defeat the right asserted, but also as respects any other available matter which might have been presented to that end.

Grubb, supra, at 478-479. (Emphasis added).

Appellant seeks to address the same issue on a ground available to it, but not

put forward for the Court's opinion, in Consumers' Counsel, supra. The issue is the same; the parties are the same; and the facts are the same. Having failed to persuade the Ohio Supreme Court through its arguments in Consumers' Counsel, supra, and this Court in Case No. 81-1002, the Appellant now wishes the same parties to relitigate the same issue based upon the same facts.

The appropriate question is how many times must we reargue the question. This Appellee most strenuously objects to a piecemeal approach to litigation. Appellant had a prior opportunity to present its arguments on the identical facts presented in the proceeding sub judice, and apparently chose not to do. so. The doctrine of res judicata compels dismissal.

Wherefore Appellee requests this Honorable Court dismiss the instant appeal.

## MOTION TO AFFIRM

Appellant has presented this Court with two grounds pursuant to which it claims plenary consideration should be given. The first related to Appellant's argument that the Ohio Supreme Court erred in its interpretation of an Ohio statute. The second argument asserts that the Ohio Supreme Court's decision in this case is in conflict with the decision of this Court in Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591 (1944). Both arguments are without merit, and this Court should affirm the ruling of the Ohio Supreme Court.

In the case sub judice, the Ohio Supreme Court dismissed an appeal by Appellant from a decision by the Public Utilities Commission of Ohio in Case No. 81-1096-EL-COI. In Case No. 81-1096-EL-COI the Commission reduced Appellant's rates in

accordance with the Ohio Supreme Court's mandate in Consumers' Counsel v. Pub. Util. Comm., 67 Ohio St.2d 153, 423 N.E.2d 820 (1981). What Appellant has sought to do is to use the instant appeal to make arguments which it failed to present in Consumers' Counsel, supra. Bearing in mind these brief comments, Appellee will now address Appellant's arguments in support of its appeal.

The underpinnings to Appellant's first jurisdictional argument rest upon the faulty premise that the expenditures associated with the cancelled plants provided service to the company's customers. Such an assertion is contrary to the specific determination of the Ohio Supreme Court in Consumers' Counsel v. Pub. Util. Comm., 67 Ohio St. 2d 153, 423 N.E.2d 820 (1981), wherein the Court stated "... what the company sought and what the commission granted, was

the amortization as service related costs of an investment that never provided any service whatsoever to the utility's customers." Id., at 164. The theory advocated by Appellant, that the expenditures somehow provided service to the ratepayers, was explicitly rejected by the Ohio Supreme Court. It is patently obvious that the expenditures never provided any service to the ratepayers.

Appellant also seeks to convince this Court that the expenditures in question were current operating expenditures. The Ohio Supreme Court soundly rejected this ploy, noting as well that the Public Utilities Commission of Ohio could not convert past losses into operating expenses by Commission fiat. Consumers' Counsel, supra, at 164.

It is axiomatic that a utility has no constitutional right to recover for past

losses. See, Bluefield Water Works Co. v. Pub. Serv. Comm. of West Virginia, 262 U.S. 679, 694 (1923). As was stated in Los Angeles Gas & Electric Corp. v. R.R. Commission, 289 U.S. 287, 313 (1933), "...Deficits in the past do not afford a legal basis for invalidating rates, otherwise compensatory, anymore than past profit can be used, to sustain confiscatory rates for the future." These expenditures were found to be past losses and not recoverable operating expenses within the meaning of Ohio Rev. Code §4909.15(A)(4).

A second problem underlying Appellant's argument hinges upon its continued reliance upon Ohio Rev. Code §4905.22. The Court's decision in Consumers' Counsel, supra, was specifically limited to "whether the cancelled plant expenditures represent (t)he cost to the utility of rendering the public utility service for the test year." Id.,

at 163. Regardless of the Appellant's assertions to the contrary, it is clear that the Ohio court strictly limited its determination as to what costs appropriately fall within the meaning of Ohio Rev. Code §4909.15(A)(4). Therefore, even if a federal question had been reviewed, it could only concern the state court's narrow holding in the case below and does not involve Ohio Rev. Code §4905.22.

The Ohio Court further found that "R.C.4909.15(A)(4) is designed to take into account the normal, recurring expenses incurred by utilities in the course of rendering service to the public for the test period." Id. Hence, it is clearly apparent that the decision below was derivative of the plain meaning of the statute's language. Appellant's investors have no statutory right to recover their investment, through amortization as service-related

costs, when that "investment***never provided any service whatsoever." Id. In reaching this holding, the Ohio Supreme Court was fairly interpreting the law of the state of Ohio. This Court should affirm the Ohio Court's decision as the United States Supreme Court has stated that state "courts have the final authority to interpret, and where they see fit, to reinterpret (their) State's legislation." Garner v. Louisiana, 368 U.S. 157, 169 (1961).

Appellant further undertakes a rather lengthy discussion regarding the applicability of a particular portion of the Uniform System of Accounts. It appears that Appellant is seeking to convince this court that, contrary to the finding in Consumers' Counsel, supra, the cost associated with the cancelled facilities are test year operating expenses. It hardly bears stating that Ohio law as interpreted by the Ohio

Court, and not the Uniform System of Accounts, governs the determination of proper test year operating expenses.

It is clear that determination of costs within the meaning of Ohio Rev. Code §4909.15(A)(4) does not present a federal question. The Ohio Supreme Court limited its decision in Consumers' Counsel, supra, to a narrow interpretation of Ohio Rev. Code §4909.15(A) which defines allowable operating expenses. The dismissal appealed from did not alter the decision in Consumers' Counsel, supra, rather it affirmed the narrow holding. As this Court stated in Durley v. Mayo, 351 U.S. 277, 281 (1956):

> It is a well-established principle of this Court that before (the Court) will review a decision of a state court it must affirmatively appear from the record that the federal question was presented to the highest court of the state having jurisdiction and that its decision of the federal question was necessary to its determination of the cause.
>
> (Emphasis added).

The Ohio Court's dismissal below, affirming Consumers' Counsel, supra, was strictly limited to a narrow issue involving Ohio Rev. Code §4909.15(A((4). There was no resolution of a federal question, nor was one called for. The decision rests upon an adequate state ground.

Where both federal and state questions have been decided by the state court, "[it] is, of course, a familiar principle that this Court will decline to review state court judgments which rest on independent and adequate state grounds, even when those judgments also decide federal questions." Henry v. Mississippi, 379 U.S. 443, 446 (1965). The rationale for the adequate state ground rule was recently reiterated by this Court in Zacchini v. Scripps-Howard Broadcasting Co.: "[O]ur only power over state judgments is to correct them to the

extent that they incorrectly adjudge federal rights." 433 U.S. 562, 566 (1977).

Therefore, due to the nonexistence of a federal question in this case this Court should affirm the decision of the Ohio Supreme Court. In addition, even if it is assumed, arguendo, that a federal question had been presented to the Ohio Supreme Court, that court rendered a decision only on a state question, thus leaving this Court with nothing over which to exercise its jurisdiction.

Without doubt the ultimate disposition of the proceeding below hinged upon the appropriate definition of the word "cost" as found in Ohio Rev. Code §4909.15(A((4). The interpretation of "cost" neither presents a federal question, nor gives rise to one. The disposition of the issue involves only state law.

Appellant's second jurisidictional argument is based upon Federal Power Commission v. Hope Natural Gas Company, 320 U.S. 591 (1941). Appellant asserts that the Ohio Supreme Court's interpretation of Ohio Rev. Code §§4909.15(A((4) and 4909.22 results in an unconstitutional deprivation of property without due process of law. The underpinning of Appellant's argument is, of course, Hope Natural Gas Co., supra, wherein the Court stated:

> The ratemaking process under the Act, i.e., the fixing of "just and reasonable" rates, involves a balancing of the investor and the consumer interests. Thus we stated in the Natural Gas Pipeline Co. Case that "regulation does not insure that the business shall produce net revenues." 315 US p 590, 86 L ed 1052, 62 S Ct 736. But such considerations aside, the investor interest has a legitimate concern with the financial integrity of the company whose rates are being regulated. From the investor or company point of view it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business... That return, moreoever, should be sufficient to assure confidence in the financial integrity of the

> enterprise, so as to maintain its credit and to attract capital. ...
>
> Hope Natural Gas Co., supra at 603.

Appellant did express in its 1979 Annual Report an opinion regarding the impact of a disallowance, as was noted in a concurring opinion in Consumers' Counsel, supra:

> CEI informed its investors in its "1979 Annual Report": "***The Company (CEI) will seek the approval of the Federal Energy Commission and the Public Utilities Commission of Ohio for authority to amortize (the costs previously expended toward the four nuclear units whose construction CAPCO terminated) over a suitable number of years. The extent to which these costs may be recovered through rates will be determined by the PUCO. If any costs of termination are not permitted to be recovered, the Company would be required to reduce net income by the disallowed amount. In any event, the resolution of these matters should not have a material adverse impact on the financial position of the Company.
>
> Id., at 171.
> (Emphasis added).

The Appellant recognized that a disallowance would not adversely impact its financial integrity. Further, it was noted

that recovery of the costs would be determined by the Public Utilities of Ohio, and ultimately, as investors are well aware, by the Ohio Supreme Court.

Appellant's investors, it must be presumed, were cognizant of and took into account the statement by Appellant that disallowance of the construction expenses should have no material adverse impact on the financial position of the company. For this reason, it cannot be suggested that the investors in CEI were unaware of the risk. As this Court noted in Bluefield Water Works Co. v. Pub. Serv. Comm. of West Virginia, 262 U.S. 683, 694 (1923), "Investors take into account the result of past operations, especially in recent years, when determining the terms upon which they will invest in such an undertaking."

By Appellant's own admission, the financial integrity of the company suffered no adverse financial impact. Further, the investors were aware of the potential for disallowance.

Appellant suggests that Hope Natural Gas Co., supra, at 606 requires; 1) that the utility be made whole for its net investment and 2) that the integrity of the investment be maintained. As to the second item it is clear from the discussion infra that Appellant's financial integrity was in no way damaged.

As to the first item, Ohio law certainly allows for the recovery of an investment when it is used and useful. The Ohio Court in Consumers' Counsel, supra, indicated that the "now terminated nuclear plants represented a major capital investment that ultimately would have been included in the rate base under R.C. 4909.15(A)(1), had the

projects not been cancelled." Id., at 164. Before capital recovery is permissible, in Ohio, a utility project must be found to be operational. "The initial risk of failure is appropriately born by the investors, who have undertaken the project and who will ultimately profit for its success. It is only proper that their venture be found operational before they commence to recoup their capital outlays from the consumers." Consumers' Counsel v. Pub. Util. Comm, 58 Ohio St.2d 449, 391 N.E.2d 311 (1979). Such treatment results in a balancing of both the investors' interest and the ratepayers' interest as Hope Natural Gas Co., supra, requires: Id., at 603.

Appellant finally suggests that Washington Gas Light Co. v. Baker, 188 F.2d 11 (D.C. Cir. 1950), Cert. den. 340 U.S. 952 (1951) is "closely analagous" to the situation presented in the case sub judice.

Such is most certainly not the case. Washington Gas Light dealt with a situation wherein a plant used in the manufacture of gas was abandoned prior to full recovery through depreciation due to a switch to natural gas. Prior to abandonment the plant in question was used in providing service. This is perhaps the most important distinction noted by the court in discussing this particular aspect;

> If a unit of property resulting from prudent investment becomes obsolete before it has been recovered in full by the investor (either through annual depreciation charges or through returns sufficient to compensate for such inadequacy), it is not necessarily erroneous as a matter of law for the Commission to include it in the rate base until such recovery has occurred...
>
> But inclusion in the rate base must meet the test of justness and reasonableness to the consumers as well as to the investor.

Id., at 19

In the present case the expenditures for which Appellant seeks recovery never provided any service whatsoever. Consumers'

Counsel, supra, at 164. Appellant seeks to have the investors insulated from all risk associated with plant construction. The rate making formula in Ohio does not permit such insulation. See, Consumers' Counsel v. Pub. Util. Comm., 58 Ohio St. 2d 449, 391 N.E.2d 311 (1979). Nor does Hope Natural Gas Co. require such a result. There has been no confiscation of property in violation of the Fifth and Fourteenth Amendments to the United States Constitution.

Therefore, Appellee, the Office of the Consumers' Counsel, submits that this Court should affirm the decision of the Ohio Supreme Court.

## CONCLUSION

Appellant in this matter has failed to timely present for review by the Ohio Supreme Court the federal constitutional questions it would now have this Court review. This Court has already found the

lack of a properly brought federal question with respect to the issues presented in this appeal, and that earlier disposition is applicable herein. Appellant is barred from further litigation of the issues by the doctrine of res judicata. This Court should, therefore, sustain Appellee's Motion to Dismiss this appeal. In the alternative, Appellee submits that the decision of the Ohio Supreme Court should be affirmed based upon Appellee's Motion to Affirm.

Respectfully submitted,

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Case No. 82-704

# In the Supreme Court of the United States

October Term, 1982

THE CLEVELAND ELECTRIC ILLUMINATING COMPANY,

*Appellant,*

vs.

THE PUBLIC UTILITIES COMMISSION OF OHIO,

and

OFFICE OF CONSUMERS' COUNSEL,

*Appellees.*

ON APPEAL FROM THE SUPREME COURT OF OHIO

## REPLY BRIEF AND SUPPLEMENTAL APPENDIX OF APPELLANT OPPOSING THE MOTION TO DISMISS OR AFFIRM

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## INTRODUCTORY STATEMENT

Appellee, Office of Consumers' Counsel (OCC), has filed a Motion To Dismiss Or Affirm (OCC Motion). This Court should overrule that Motion and allow plenary consideration.

Setting aside the conflicting positions taken by OCC in the several proceedings concerning this matter, what is *not* disputed deserves emphasis. OCC does not dispute that Appellant, The Cleveland Electric Illuminating Company (CEI), prudently initiated construction of four electric generating units, prudently spent $56.4 million planning and engineering them, and prudently cancelled them on January 23, 1980. OCC does not dispute that Ohio Revised Code Section 4905.22 requires CEI to provide adequate service and facilities in the future, nor that base load generating units take a decade or more to build. OCC does not dispute that the Uniform System of Accounts incorporated in the Ohio Administrative Code required CEI to postpone recovery through rates *of* the $56.4 million until the units went into service. OCC does not dispute that the same Uniform System of Accounts provided for the recovery *of* these costs if the units had to be abandoned before the investor had obtained recovery of his investment through accumulated depreciation. (*See* Account 182, quoted in full in CEI Jurisdictional Statement, p. 18).

Indeed, OCC does not dispute that the validity of Ohio Revised Code Sections 4905.22 and 4909.15(A)(4), as construed in *Consumers' Counsel v. Pub. Util. Comm. (CEI)*, 67 Ohio St.2d 153 (1981)[1] and applied to CEI in *this* case, was "drawn into question" before the Ohio Supreme Court on grounds that they are repugnant to the Fifth and Fourteenth Amendments, and that the decision of the Ohio Supreme Court below was in favor of the

[1] Reprinted in CEI's Appendix at pages H-1 through H-24. Hereinafter cited as *Consumers' Counsel*.

validity of those statutes as construed and applied. OCC expressly admits (Motion, p. 29) that the dismissal below "affirmed" the decision in *Consumers' Counsel.*

OCC admits (p. 18) that the COI Order of the Public Utilities Commission of Ohio (Commission) here appealed *"reduced Appellant's rates,* removing therefrom the expenditures associated with the terminated nuclear units." (Emphasis added). Finally, OCC does not even dispute the *substantiality* of the constitutional question presented. If the Ohio statutes, as construed and applied, are confiscatory, as Appellant contends here, then the confiscation has now occurred. Appellant CEI respectfully submits that the monumental importance of this case to CEI and the utility industry requires plenary consideration by this Court.

## ARGUMENT

### I. THE DOCTRINES OF *RES JUDICATA* AND COLLATERAL ESTOPPEL ARE TOTALLY INAPPLICABLE TO THIS CASE.

OCC presents arguments which are all variations on *res judicata* or, perhaps more correctly, collateral estoppel themes. OCC asserts (OCC Motion, pp. 7-16) that this Court's dismissal of CEI's appeal from *Consumer's Counsel* "for want of a properly presented federal question" (Case No. 81-1002; 71- L.Ed. 2d 455) was a decision "on the merits (OCC Motion, p. 16) of the constitutional issue CEI is now placing before this Court. This contention, of course, is baseless. In citing and relying on *Hicks v. Miranda,* 422 U.S. 322 (1975), OCC conveniently overlooks the fact that the Court was addressing the effect of a dismissal "for want of a *substantial* federal question" (emphasis in the original) and, moreover, that the Court carefully premised its discussion by stating that "[a] federal constitutional issue [had been] properly presented" in that case. Obviously, therefore, nothing in *Hicks* can be read to support OCC's claim that a dismissal

"for want of a properly presented federal question" is a determination on the merits. *See* R. STERN AND E. GRESSMAN, SUPREME COURT PRACTICE, 380-381 (5th ed. 1978).[2] This Court has not decided the substantial federal question raised by CEI here.[3]

*This* appeal is from an entirely new and different case from the one which this Court considered in Case No. 81-1002. The reasons for this Court's prior dismissal have no bearing on *this* case since the dismissal was *not* on the merits.

OCC's claim (Motion, p. 13) that "The COI Order was merely a continuation of the earlier proceedings requiring compliance with the Ohio Court's mandate" is wrong, both factually and legally. As Exhibit I to Appellant's Jurisdictional Statement shows, *Consumers' Counsel* and Case No. 81-1002 before this Court were appeals from CEI's 1979 Case, the 1980 Case superseded[4] those rates, and the COI case reducing the 1980 rates is before this Court in *this* proceeding.[5]

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[2] *See also Colorado Springs Amusements, Ltd. v. Rizzo*, 428 U.S. 913, 914 n.1 (1976, Justice Brennan dissenting); *Doe v. Delaware*, 450 U.S. 382, 383 n.4 (1981, Justice Brennan dissenting).

[3] OCC also assumes that this Court previously dismissed "for want of a properly presented federal question" because the confiscation question was allegedly raised on rehearing and was, therefore, too *late*. It could well be argued that the prior appeal was too *early*, since the decision in *Consumers' Counsel* lacked finality. Since that decision "remanded" to the Commission for a "redetermination" of CEI's allowable expenses (CEI Appx., H-20), plainly the way remained open for the Commission "to set a profitable rate . . . which might well satisfy the losing party to acquiesce in the disposition of the earlier issue." *Republic Natural Gas Co. v. Oklahoma*, 334 U.S. 62, 71 (1948). *See also State of Ohio v. The Western Union Tel. Co.*, 154 Ohio St. 511, 97 N.E.2d 2 (1951).

[4] 67 Ohio St. 2d 153, 154 n.3, CEI Appx. H-3.

[5] The Commission simultaneously initiated a Commission Ordered Investigation into Toledo Edison's existing rates, which is discussed *infra*.

The Commission concluded that an investigation of the *1979* rates that had been before the Ohio Court in *Consumers' Counsel* "would be a meaningless exercise." (COI Order, CEI Appx. E-4). Instead, the Commission chose "to implement the Supreme Court's mandate through the *initiation* of this *proceeding.*" (COI Order, CEI Appx. E-4). The Commission found that it could do so pursuant to Ohio Revised Code Section 4905.26 despite the facts that the 1980 rates "are presumptively just and reasonable" and that "there is no remand or mandate" in the 1980 Case. (COI Order, CEI Appx. E-5). In reducing CEI's 1980 rates here, the Commission was well aware that those rates had been set using a calendar 1980 test year (COI Order, CEI Appx. E-5) and that the 1979 rates, "remanded" in *Consumers' Counsel,* had been set using a calendar 1979 test year (CEI Appx., J-3). OCC's assertion of *res judicata* is thus wholly without foundation. In *this* case, the confiscation has plainly occurred, CEI is "out of pocket," and the decision is final.

Legally, it is settled in Ohio that a proceeding initiated by the Commission to investigate the reasonableness of a utility's existing rates pursuant to Ohio Revised Code Section 4905.26, as the Commission did below, is "*not* a rehearing or a continuation of [a] prior application for a rate increase" but is "*a separate investigation.*" *Ohio Utilities Co. v. Pub. Util. Comm.*, 58 Ohio St. 2d 153, 159, 389 N.E. 2d 483, 487 (1979, emphasis added). *Ohio Utilities* was relied upon for precisely this proposition when the Ohio Court affirmed the Commission's initiation of a Section 4905.26 proceeding[6] to investigate "the reasonableness of [Toledo Edison's] rate schedules in the light of *new law,* such as our decision in *Consumers' Counsel,*

[6] Toledo Edison was not a party in *Consumers' Counsel* but its existing rates included an amortization of its investment in these same cancelled plants. *See Toledo Edison Co.*, 42 PUR 4th 568, 589 (1981).

*supra.*" *Consumers' Counsel v. Pub. Util. Comm.* (*Toledo Edison*), 1 Ohio St.3d 22, 24, 437 N.E.2d 586, 588 (1982).

The present case for CEI is a new and separate cause of action, exactly like the Commission Ordered Investigations of *Ohio Utilities* and of *Toledo Edison*,[1] and the doctrine of *res judicata* is not applicable. *Norwood v. McDonald*, 142 Ohio St. 299, 52 N.E.2d 67 (1943).

OCC is also plainly wrong in stating that this appeal "seeks to relitigate *the same issue* based upon the same facts." (OCC Motion, p. 22). As this Court itself has said in the context of income tax issues that arise in different tax years, "Each year is the origin of a new liability and of a separate cause of action." Thus, a judgment addressing an issue in one year is *res judicata* only in a proceeding "*involving the same claim and the same tax year.*" *Commissioner v. Sunnen*, 333 U.S. 591, 598 (1948, emphasis added). Indeed, the Ohio Court has adopted the same approach. *Beatrice Foods Co., Inc. v. Lindley*, 70 Ohio St.2d 29, 434 N.E.2d 727, 731 (1982). In parallel fashion, this case involves a different rate year from that before the courts in *Consumers' Counsel* and, thus, the question before the Ohio Court and this Court plainly involves "a new liability and . . . a separate cause of action." *Sunnen, supra.*

Likewise, even assuming that the doctrine of collateral estoppel may be applied to questions of law in addition to questions of fact, "collateral estoppel [applies] only as to those matters . . . which were actually presented and determined in the first suit." *Sunnen, supra.* Since the Ohio Court has never addressed the federal issue, which has been "drawn in question" at every available opportunity

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[1] The Commission's refusal to reduce Toledo Edison's rates after this Investigation plainly belies OCC's claim (Motion, p. 1) that the Commission's decisions in these Investigations were mere "mechanical manifestation[s]" of *Consumers' Counsel.*

*since* the Ohio Court announced this "new law,"[8] collateral estoppel cannot possibly apply.[9] CEI unequivocably argued in *this* case that its property had been confiscated, and *OCC does not deny it.*[10]

Even assuming the federal question was presented to the Ohio Court too late in *Consumers' Counsel,* surely that fact does not relieve the Ohio Court from considering the question in all subsequent cases, for all time, as OCC seems to imply, nor should it prevent this Court from *ever* considering the question when it is properly presented in such subsequent cases.[11]

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[8] *Consumers' Counsel v. Pub. Util. Comm. (Toledo Edison),* 1 Ohio St.3d 22, at 24, 437 N.E. 2d 586, 588 (1982).

[9] The *Commission* has never addressed the constitutionality of the statutes, as construed and applied, because it does not have jurisdiction to do so. *Panhandle Eastern Pipe Line Co. v. Pub. Util. Comm.,* 56 Ohio St.2d 334, 337, 383 N.E.2d 1163, 1165 (1978). Moreover, OCC can hardly assert that the Ohio Court implicitly decided the constitutional issue previously in *Consumers' Counsel* in light of its argument to the opposite effect to this Court in that case. *See also* OCC Motion, p. 6, admitting that the Ohio Court had *not* decided the constitutional question.

[10] On appeal to the Ohio Court in this case, CEI's Proposition of Law No. 2 stated:

> "Ohio Revised Code § 4905.22 and § 4909.15(A)(4), as construed by this Court, directly conflict with the proscription of the Fifth and Fourteenth Amendments to the Constitution of the United States prohibiting confiscation of private property without due process of law."

Proposition of Law No. 3 stated:

> "Ohio Revised Code § 4905.22 and § 4909.15(A)(4), as construed, directly conflict with the Supreme Court's decision in *Federal Power Commission v. Hope Natural Gas Co.,* 320 U.S. 591 (1944)."

[11] Likewise, the doctrine of 'law of the case' also does not affect this Court's jurisdiction here. Even a ruling by the State court that an earlier decision constitutes the law of the case does not deprive this Court of jurisdiction to reexamine the question. *Davis v. O'Hara,* 266 U.S. 314, 321 (1924); *Reece v. Georgia,* 350 U.S. 85, 87 (1955); *Hathorn v. Lovorn,* 50 U.S. L.W. 4664 (1982).

## II. AS APPLIED BELOW TO REDUCE APPELLANT'S RATES, OHIO REVISED CODE SECTIONS 4905.22 AND 4909.15(A)(4) CONFISCATE APPELLANT'S PROPERTY WITHOUT DUE PROCESS OF LAW.

OCC's attention to the merits is short, but inaccurate. OCC argues (p. 38) that CEI seeks to have the investors "insulated from all risk" associated with plant construction. That argument is totally false. CEI sought recovery *of* the $56.4 million actually spent planning and engineering these units. CEI did *not* seek and has never sought "profit" *on* that $56.4 million. The *undisputed* testimony of CEI witness Maugans in the 1979 Case (CEI Ex 4A, p. 27) showed that a ten year amortization, without rate base treatment, would produce a nearly equal sharing of the burden between the ratepayer and the investor. Simply put, the Commission's Order in the 1979 Case took from the investor the time value of his prudently invested money for the next ten years (the amortization period), but allowed the investor eventually to recover his actual prudent investment.[12] The Ohio Court reversed that treatment in *Consumers' Counsel*. The Commission's COI Order, here under appeal, then confiscated that actual investment ($56.4 million) from the investor by removing

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[12] This proposition has been adopted in virtually every case decided on this subject, and they are cited in the Table of Authorities of CEI's Jurisdictional Statement. *See particularly Virginia Electric & Power Co.*, 29 PUR 4th 65 (Virginia State Corp. Comm., 1979, discussing the allowed amortization at page 76 and the denial of rate base treatment at page 80; Commissioner Shannon's dissent from this denial at pages 95-97 was quoted to the Ohio Court in CEI's first brief in *Consumers' Counsel*); *NEPCO Mun. Rate Comm. v. Fed. Energy Reg. Comm.*, 668 F.2d 1327, 1333-1335 (D.C. Cir., 1981), *cert. den.* 50 U.S.L.W. 3978 (1982); *Central Maine Power Co. v. Pub. Util. Comm.*, 433 A.2d 331, 344-345 (Maine Supreme Court, 1981); *Rochester Gas & Electric Corp.*, 45 PUR 4th 386, 403-411 (N.Y. Pub. Serv. Comm., 1982).

that one line-item of cost from rates without any consideration of any other changes in revenues, expenses, rate base or rate of return. The Ohio Court dismissed Appellant's appeal without opinion. The issue here is whether the State of Ohio may constitutionally *require* utilities to invest in generating units which take ten or more years to build, *require* postponement of recovery through rates, and then refuse any recovery *at all of* the capital outlay – not a profit on it – even where it was *prudently* made.[13] *See* Ohio Revised Code Section 4909.154.

OCC errs when it argues (p. 26) that only Ohio Revised Code Section 4909.15(A)(4) is involved here. The Ohio Court itself assumed that Section 4905.22 "impose[d] a duty" on CEI to make these expenditures "to plan for the future." (67 Ohio St.2d at 164; CEI Appx. H-14). Without Section 4905.22, CEI would not have had a statutory duty to risk this capital to build sufficient generating capacity for the future. CEI would not have had to make the hard choice to build, or not to build.

OCC misses the point when it argues (pp. 26-31) that the Ohio Court strictly limited its determination in *Consumers' Counsel* to construing Ohio statutes, and, therefore, no federal question is presented here. By that test, no

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[13] Assume that demand for electricity is projected to grow at a certain rate, requiring the construction of a new generating unit. Ohio Revised Code Section 4905.22 requires an Ohio utility to begin construction. Under present Ohio law, the utility is "damned if it does and damned if it does not." If construction is begun, the costs may not be recovered currently, but must be deferred and charged to the project. If growth in demand then slows, making it prudent to cancel, the utility loses no matter what it does. Under Ohio law as now construed, if the project is continued, the unit could be excluded from rate base as "excess capacity" (R.C. § 4905.70) and, therefore, not "used and useful" property (R.C. § 4909.15(A)(1). The entire investment is then lost. If the utility prudently cancels, the utility loses the accumulated costs which had been deferred and charged to the project, under *Consumers' Counsel*. This classic "Catch-22" is unconstitutional.

state court decision involving a state statute would be reviewable by this Court unless the state court chose to address the constitutional issue. 28 U.S.C. 1257(2) is not so limited.

On the other hand, OCC properly admits that the Ohio Court's dismissal of CEI's appeal here necessarily "affirmed" *Consumers' Counsel* as applied. (OCC Motion, p. 29). It surely did, in the face of an explicit constitutional challenge to Ohio Revised Code Sections 4905.22 and 4909.15(A)(4) as newly construed in *Consumers' Counsel* and then *applied* in the Commission's COI Order. The record as a whole in *this* case clearly shows that "the federal claim was brought to the attention of the state court with fair precision and in due time." *New York ex rel. Bryant v. Zimmerman*, 278 U.S. 63, at 67 (1928); *Street v. New York*, 394 U.S. 576, 581-585 (1969); *Henry v. Mississippi*, 379 U.S. 443 (1965); *Chambers v. Mississippi*, 410 U.S. 284 (1973). The Ohio Court may not deprive this Court of jurisdiction by the simple expedient of refusing to pass on the federal question.

OCC's argument (pp. 32-39) that no confiscation has occurred because CEI's 1979 Annual Report predicted that "the resolution of these matters should not have a *material* adverse impact on the *financial position* of the Company" is erroneous. That statement addressed the SEC's *balance sheet* test, certainly not this Court's test for confiscation. The Commission's COI Order, appealed here, requires a one-time write-off of $32 million, 20% of 1981 net *earnings*, unless this Court acts. That is plainly confiscation. *Bluefield Water Works v. Pub. Serv. Comm.*, 262 U.S. 679 (1923); *West Ohio Gas Co. v. Pub. Util. Comm. (No. 1)*, 294 U.S. 63 (1935); *Fed. Pwr. Comm. v. Hope Natural Gas Co.*, 320 U.S. 591 (1944); *Mississippi River Fuel Corp. v. Fed. Pwr Comm.*, 163 F.2d 433, at 437 (1947).

## CONCLUSION

In its COI Order the Commission declined to examine the impact of disallowance as an expense of the costs associated with the cancelled plants on the other parts of the ratemaking formula (revenues, expenses, rate base and rate of return) and removed this expense from the rates it found fair and reasonable in Appellant's 1980 Case. The confiscation has occurred and the result is final unless this Court acts. This case presents this Court with a clear-cut issue: Is it constitutional for Ohio to require prudent investment by a public utility to insure adequate service and facilities and simultaneously to prohibit the utility from any opportunity whatsoever for recovery *of* that prudent investment? The Ohio statutes, which require such a result as construed and applied here, plainly confiscate the utility's property.

For the foregoing reasons, the questions presented are so substantial as to require plenary consideration, with briefs on the merits and oral argument, for their resolution, and the Motion To Dismiss Or Affirm should be denied.

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## SUPPLEMENTAL APPENDIX

### § 4905.26 Complaints as to service. (GC § 614-21)

Upon complaint in writing against any public utility by any person, firm, or corporation, or upon the initiative or complaint of the public utilities commission, that any rate, fare, charge, toll, rental, schedule, classification, or service, or any joint rate, fare, charge, toll, rental, schedule, classification, or service rendered, charged, demanded, exacted, or proposed to be rendered, charged, demanded, or exacted, is in any respect unjust, unreasonable, unjustly discriminatory, unjustly preferential, or in violation of law, or that any regulation, measurement, or practice affecting or relating to any service furnished by said public utility, or in connection with such service, is, or will be, in any respect unreasonable, unjust, insufficient, unjustly discriminatory, or unjustly preferential, or that any service is, or will be, inadequate or cannot be obtained, and, upon complaint of a public utility as to any matter affecting its own product or service, if it appears that reasonable grounds for complaint are stated, the commission shall fix a time for hearing and shall notify complainants and the public utility thereof, and shall publish notice thereof in a newspaper of general circulation in each county in which complaint has arisen. Such notice shall be served and publication made not less than fifteen days nor more than thirty days before hearing and shall state the matters complained of. The commission may adjourn such hearing from time to time.

The parties to the complaint shall be entitled to be heard, represented by counsel, and to have process to enforce the attendance of witnesses.

Upon the filing of a complaint by one hundred subscribers or five per cent of the subscribers to any telephone exchange whichever number be smaller, or by the legislative authority of any municipal corporation served

by such telephone company that any regulation, measurement, standard of service, or practice affecting or relating to any service furnished by said telephone company, or in connection with such service is, or will be, in any respect unreasonable, unjust, discriminatory or preferential, or that any service is, or will be inadequate or cannot be obtained, the public utilities commission shall fix a time for the hearing of such complaint.

The hearing provided for in the next preceding paragraph shall be held in the county wherein resides the majority of the signers of such complaint, or wherein is located such municipal corporation. Notice of the hearing shall be served upon the telephone company complained of, upon each municipal corporation served by said telephone company in the county or counties affected, and shall be published for not less than three consecutive weeks in a newspaper of general circulation in the county or counties affected.

Such hearing shall be held not less than fifteen nor more than thirty days after the third publication of such notice.

HISTORY: GC § 614-21; 102 v 549(556), § 23; 125 v 613(616). Eff 10-26-53.

**§ 4905.70** [Energy conservation programs.]

The public utilities commission shall initiate programs that will promote and encourage conservation of energy and a reduction in the growth rate of energy consumption, promote economic efficiencies and take into account long-run incremental costs. Notwithstanding sections 4905.31, 4905.33, 4905.35, and 4909.151 [4909.15.1] of the Revised Code, the public utilities commission shall examine and issue written findings on the declining block rate structure, lifeline rates, long-run incremental pricing,

peak load and off-peak pricing, time of day and seasonal pricing, interruptible load pricing, and single rate pricing where rates do not vary because of classification of customers or amount of usage. The public utilities commission shall establish criteria for the investigation, identification, and remedy of the existence of any *excess capacity* in the generating systems of electric light companies. The public utilities commission, by a rule adopted no later than October 1, 1977, and effective and applicable no later than November 1, 1977, shall require each electric light company to offer to such of their residential customers whose residences are primarily heated by electricity the option of their usage being metered by a demand or load meter. A customer who selects such option may, under the rule, be required by the company, where no such meter is already installed, to pay for such meter and its installation. The rule shall require each company to bill such of its customers who select such option for those kilowatt hours in excess of a prescribed number of kilowatt hours per kilowatt of billing demand, at a rate per kilowatt hour that reflects the lower cost of providing service during off-peak periods.

HISTORY: 137 v H 230. Eff 10-9-77. (Emphasis added).

[§ 4909.15.4] § 4909.154 [Consider management policies, practices and organization.]

In fixing the just, reasonable, and compensatory rates, joint rates, tolls, classifications, charges, or rentals to be observed and charged for service by any public utility, the public utilities commission may consider the management policies, practices, and organization of the public utility. The commission may require such public utility to supply information regarding its management policies, practices, and organization.

## SUPPLEMENTAL APPENDIX

If the commission finds after a hearing that the management policies, practices, or organization of the public utility are inadequate, inefficient, or improper, the commission may recommend management policies, management practices, or an organizational structure to the public utility.

In any event, the public utilities commission shall not allow such operating expenses of a public utility as are incurred by the utility through management policies or administrative practices that the commission considers *imprudent*.

HISTORY: 136 v S 94. Eff 9-1-76. (Emphasis added).